

# Pursuing Competition and Regulatory Reforms for Achieving Sustainable Development Goals





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Reforms for Achieving Sustainable  
Development Goals

# Pursuing Competition and Regulatory Reforms for Achieving Sustainable Development Goals

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Tel: +91.141.2282821, Fax: +91.141.2282485

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In view of this overall aim of the project, with inputs from the project advisers CUTS designed the final conference of the CREW project on a broader theme to talk about ‘Relevance of Competition & Regulatory Reforms in Pursuing Sustainable Development Goals (SDGs) in Developing Countries’. The theme was thought to be both contemporary and relevant in view of the adoption of the SDGs a couple of months before this final conference. In addition to the support it received from DFID (UK), BMZ (Germany) and GIZ (Germany), the conference also received support from the World Bank, G-77 Secretariat and the OECD. CUTS is grateful to all the above organisations for supporting the conference, and indeed also the production of this volume.

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**Rijit Sengupta**  
Project Coordinator

# Abbreviations

ADB	: Asian Development Bank
AMC	: Antimonopoly Committee
AMU	: Arab Maghreb Union
ANC	: African National Congress
AoD	: Abuse of Dominance
APEC	: Asia Pacific Economic Cooperation
ASEAN	: Association of South East Asian Nations
ATAs	: Agency-to-Agency Agreements
BNDES	: Brazil National Bank for Economic and Social Development
BRTF	: Better Regulation Task Force
BTIAs	: Broad Trade and Investment Agreements
CADE	: Conselho Administrativo de Defesa Econômica
CARICOM	: Caribbean Community
CAs	: Competition Authorities
CCC	: COMESA Competition Commission
CCJ	: COMESA Court of Justice
CCMP	: Colonial Capitalist Mode of Production
CEMAC	: Central African Economic and Monetary Community
CEPA	: Comprehensive Economic Partnership Agreement
CEPGAL	: Economic Community of the Great lakes Countries
CER	: Closer Economic Relations Agreement between Australia and New Zealand
CFC	: Federal Competition Commission (Mexico)
CFTA	: Continental Free Trade Area
CFTC	: Competition and Fair Trade Commission
CIC	: Technological Research Commission
CMV	: Common Method Variance
COMESA	: Common Market for Eastern and Southern Africa

DCs	: Developing Countries
DoT	: Department of Telecommunications
DRC	: Democratic Republic of Congo
EAC	: East African Community
EC	: European Commission
ECCAS	: Economic Community for Central African States
ECOWAS	: Economic Community of West African States
EFA	: Education for All
ERPs	: Economic Recovery Programmes
EU	: European Union
EWURA	: Energy and Water Utilities Regulatory Authority
FCA	: Fair Competition Act
FCC	: Fair Competition Commission
FDI	: Foreign Direct Investment
FLEC	: Federal Law on Economic Competition
FNE	: Fiscalía Nacional Económica
FTAs	: Free Trade Agreements
GATT	: General Agreement on Tariffs and Trade
GCR	: Global Competition Review
GDP	: Gross Domestic Product
GEAR	: Growth, Employment and Redistribution
HHI	: Herfindahl–Hirschmann Index
ICN	: International Competition Network
ICT	: Information and Communication Technology
IFC	: International Finance Corporation
IFETEL	: Federal Institute of Telecommunications
IMF	: International Monetary Fund
IPRs	: Intellectual Property Rights
IR	: International Relations
ISI	: Import Substitution Industrialisation
JSSCE	: Junior Secondary School Certificate Examination
LDCs	: Least Developing Countries

M&As	: Mergers & Acquisitions
MDGs	: Millennium Development Goals
MEMEs	: Micro, Small and Medium-Sized Enterprises
MERCOSUR	: Mercado Comun del Sur
MNCs	: Multinational Corporations
MLATs	: Mutual Legal Assistance Treaties
MoU	: Memorandum of Understanding
MSCAs	: Member State Competition Authorities
NAFTA	: North American Free Trade Agreement
NCC	: National Communications Commission
NERA	: National Economic Research Associates
NSEP	: National Economic Survival Programme
OECD	: Organisation for Economic Cooperation and Development
OTT	: Over-The-Top
PBA	: Province of Buenos Aires
PEA2	: Participative Agri-food and Agribusiness Strategic Plan
PEI	: Strategic Industrial Plan
PEPBA	: Strategic Productive Plan Buenos Aires
PPP	: Public-Private Partnership
PROFECO	: Office of the Federal Prosecutor for the Consumer
R&D	: Research & Development
RCAs	: Regional Competition Authorities
RCC	: Regulatory Cooperation Council
RCEP	: Regional Comprehensive Economic Partnership
RDP	: Reconstruction and Development Programme
RDTs	: Regulatory Decision Tools
RIAs	: Regional Integration Arrangements
RTAs	: Regional Trade Agreements
SACU	: Southern Africa Customs Union
SADC	: Southern Africa Development Community
SAP	: Structural Adjustment Programme
SDGs	: Sustainable Development Goals
SECOFI	: Secretary of Commerce and Industrial Development

SMEs	:	Small and Medium Enterprises
SMPs	:	Two-sided Market Platforms
SSCE	:	Senior School Certificate Examination
STEM	:	Science, Technology, Engineering and Mathematics
SUMATRA	:	Surface and Marine Transport Regulatory Authority
TANROADS	:	Tanzania National Roads Agency
TAOMAC	:	Tanzania Oil Marketing Companies
TCAA	:	Tanzania Civil Aviation Authority
TCRA	:	Tanzania Communications Regulatory Authority
TDLC	:	<i>Tribunal de Defensa de la Libre Competencia</i>
TELCEL	:	TELMEX and RadioMóvil Dipsa
TFTA	:	Tripartite Free Trade Area
TMSA	:	Trade Mark Southern Africa
TPP	:	Trans-Pacific Partnership
TTIP	:	Transatlantic Trade and Investment Partnership
UABI	:	University-Associated Business Incubators
UBE	:	Universal Basic Education
UBIs	:	University-Based Incubators
UEMOA	:	West African Economic and Monetary Union
UNCTAD	:	United Nations Conference on Trade and Development
UNDP	:	United Nations Development Programme
UPE	:	Universal Primary Education
VIF	:	Variance Inflation Factor
WAEMU	:	West African Economic and Monetary Union
WB	:	World Bank
WTO	:	World Trade Organisation



# Contributors

## **Afolayan Gbenga Emmanuel**

Afolayan Gbenga Emmanuel is currently a Doctoral Candidate at School of Education, Murdoch University Australia. He holds two master's degrees. The first, a Masters in Development Studies, from International Institute of Social Studies of Erasmus University Rotterdam, the Netherlands and the second is a Master's in Public Policy and Management, from University of York, UK. Also, Gbenga had a bachelor degree of Education in Counselling Psychology and Economics from University of Ibadan, Nigeria. Gbenga's research interests fall in the areas of education and social inequalities, development policies and administration, sociology of education/development, women studies, feminist economics, human rights and social justice. He taught Economics and Business Management for more than five years at the Federal Polytechnic Ilaro, Ogun State, Nigeria.

## **Clayton Hazvinei Vhumbunu**

Clayton Hazvinei Vhumbunu is an Associate Researcher with the Southern African Research and Documentation Centre, Harare; Zimbabwe. He is concurrently a PhD Candidate in International Relations at the University of KwaZulu-Natal in Durban; South Africa. He is a Zimbabwean by nationality. His research interests are in International Relations, Regional Integration and International Trade, and Public Policy. Clayton holds an Msc in International Relations and Bsc (Hons) in (Political) Administration (both from the University of Zimbabwe); Diploma in Community Development (TDI, Zimbabwe); Post-Graduate Certificate in International Trade and Development (Lund University/Trapca; Tanzania); Certificate in Public Policy, Governance and Leadership (OSISA/Africa University; Zimbabwe).

**Deo John Nangela**

Deo John Nangela is Director of Restrictive Trade Practices at the Fair Competition Commission, Tanzania. He is also a part-time lecturer at the University of Dar-es-Salaam School of Law and an advocate of the High Court of Tanzania. Deo has been senior state counsel with the Attorney General's Chambers before joining staff of the School of Law, University of Dar es Salaam. He joined the FCC in 2011.

**Derek Ireland**

Derek Ireland has been a Senior Economist and Manager in the Canadian public and private sectors for over four and a half decades. He has a BA in Economics and Asian Studies from the University of British Columbia in 1968, an MA in Economics from Carleton University, which he received in the mid-1970s; and he returned to university in the Fall of 2003 as a student in the PhD programme in Public Policy at Carleton University in Ottawa Canada, and received his PhD in February 2009. His PhD research and dissertation was on the evolution of competition policy and law in India and the interactions with the country's business community, especially its business groups. In recent years, Dr. Ireland has been operating his own policy consulting firm and has been a Lecturer and Fellow at the Arthur Kroeger College at Carleton.

**Federico Del Giorgio Solfa**

Federico Del Giorgio Solfa is an Industrial Designer, Professor in Industrial Design, Master of International Marketing and Full Professor of Project Management at the National University of La Plata. He is Master in Law, Economy and Politics of European Union at the University of Padova; full Professor of Local Development in the Master of Labor Relations at the National University of Lomas de Zamora; and visiting Professor of Advanced Seminar in Design I for the Doctorate in Design at University of Palermo.

**Frederic Ringo**

Frederic Ringo is Director General at the Fair Competition Commission of Tanzania. He has been in government as principal counsel for the privatisation commission. He has also been chief legal counsel for the African Export Import Bank in Cairo, Egypt, before practicing as a private practitioner. He joined the FCC in 2013.

**Kuo-Tai Cheng**

Kuo-Tai Cheng is Associate Professor of Public Administration and Policy at the National Hsin-chu University of Education in Taiwan. He works on issues of public utility privatisation, regulatory governance, governance mechanism, regulatory capture, governance mechanism, organisational behaviour, and human resource development. His latest books in Chinese are ‘Regulatory Governance: Theory and Practice’ and ‘Public Governance’.

**María Sol Sierra**

She is an Industrial Designer and Professor in Industrial Design at the National University of La Plata, where she was Assistant Professor in Industrial Design I and Technology for Industrial Design I. She is currently pursuing PhD in Latin American Contemporary Art at the same University; and she is an Improvement Scholar Researcher at the Department of Industrial Design of the National University of La Plata, for the Scientific Research Commission of the Buenos Aires province.

**Paul Kinuya**

Paul Kinyua has taught law at The Catholic University of Eastern Africa in Nairobi, Kenya since 2012. He holds a Bachelor of Laws (LLB, Hons.) from Moi University, Kenya; and a Master of Laws (LLM) in International Trade Law from Stellenbosch University, South Africa where he is currently a doctoral student. His doctoral research concerns the regulation of multinational corporations by African States. He is also an Advocate of the High Court of Kenya.

**Rachel Glanz**

Rachel Glanz is a student at Duke University, completing a Bachelor’s (B.A.) degree in Political Science and a certificate in Politics, Philosophy and Economics (PPE), with an honors thesis on the topic of campaign finance at the US Congressional level.

**Rodrigo de Camargo Cavalcanti**

Rodrigo de Camargo Cavalcanti holds a Doctor in Law and Master in Law by the Pontifícia Universidade Católica de São Paulo. He is a researcher at National Foundation of Development of the Private Higher Education (FUNADESP); Professor at Faculdades Alves Faria (ALFA) and Press and Communication Director of the Law Post-Graduating Students Association of the Pontifícia Universidade Católica de São Paulo (APGDireito/PUC-SP).

**S Chakravarthy**

S Chakravarthy is a Civil Servant by profession, being a Member of the Indian Administrative Service. He is a Master's Degree holder in Mathematics and Statistics having stood First Class First in the University. After joining the Government, he got a Doctorate Degree in Management from the Indian Institute of Technology, Delhi. Subsequently, he secured a Law Degree from the Delhi University. In addition, he has certificates in Public Administration and Public Enterprises from the University of Manchester, UK and Harvard University, US. Among the top assignments he held were Special Chief Secretary to Government and Member, Monopolies and Restrictive Trade Practices Commission (MRTPC). As Member, Company Law Board and Member, MRTPC, his experience as adjudicating Tribunal is around 10 years. Presently, he is Adviser/Consultant on Competition Policy and Law.

**Seema Gaur**

Seema Gaur is a Federal Government Economist belonging to Indian Economic Service with more than 30 years of experience in key economic Ministries. Apart from Economics, she is also having a degree in Law as well as public administration. Presently, she is working as Economic Adviser in the Department of Industrial Policy and Promotion, Ministry of Industry and Commerce, Government of India. Prior to this, she was Adviser in the Competition Commission of India (CCI) for about six and a half years since May, 2009, when implementation of Competition Law started in India. She was also India's lead negotiator in negotiations for Competition Chapter in trade and investment agreements with EU, EFTA and RCEP. She has presented papers in many international conferences, published papers in peer reviewed journals as well research done for the UNCTAD's Research Partnership Platform and written chapters in books on key economic issues including competition law and policy.

**Surajit Deb**

Surajit Deb did his Ph. D. in Economics from Department of Economics, Delhi School of Economics, University of Delhi, in 2003 in the area of Macroeconomic Implications of Agricultural Price Movements and Time Series Econometrics. He has published extensively in academic journals, participated in international conferences and completed commissioned research projects for international organisations. He has acted as a member of the Working Group on Terms of Trade between the Agricultural and Non-agricultural Sectors during 2012-15 for the Ministry of Agriculture:

Government of India, and is empanelled in the ICSSR Research Pool of Research Methodology Experts. He is working as an Associate Professor in Aryabhata College (University of Delhi) and his current interests include construction of Social Development Index for Indian states, analysis on inclusive growth and India-China comparisons.

**Tim Buthe**

Tim Büthe is Associate Professor of Political Science and Public Policy, as well as a Senior Fellow of the Kenan Institute for Ethics at Duke University. He leads the Competition Law and Policy Project of Duke's Rethinking Regulation Programme and directs a major research project about competition law and policy in comparative perspective. He also is guest editor (with Umut Aydin) of the Autumn 2016 issue of *Law and Contemporary Problems* about 'Competition Law and Policy in Developing Countries.' In 2015, he was the first political scientist (with Cindy Cheng) appointed to the World Bank-OECD Global Network of Experts on Competition and Shared Prosperity.

**Umut Aydin**

Umut Aydin is Assistant Professor of Political Science at the Universidad Católica de Chile, Santiago. She has a PhD in Political Science from University of Washington, Seattle, and an MA degree from McGill University, Canada. She was a post-doctoral fellow at the European University Institute, Italy, and a George C. Lamb Jr. Fellow in Regulatory Governance at Duke University's Kenan Institute for Ethics. Her research lies at the intersection of comparative and international political economy, and is focussed broadly on regulatory politics in a globalising world. Her current research focusses on competition law and policy in developing countries, especially in Turkey, Mexico and Chile. Her published work on competition law and policy includes articles and chapters on EU's external relations in competition policy, the International Competition Network, and Turkish competition law and policy.

**Varadharajan Sridhar**

Varadharajan Sridhar is Professor at the Centre for IT and Public Policy at the International Institute of Information Technology Bangalore, India. He has published many articles in peer-reviewed leading telecom and information systems journals. He is the author of two books published by the Oxford University Press. Sridhar has taught at Ohio University and American University, US; University of Auckland, New Zealand; Indian

Institute of Management Lucknow, Management Development Institute Gurgaon, India. He was also a visiting scholar at Aalto University, Finland and was the recipient of Nokia Visiting Fellowship. He has written more than 200 articles in prominent business newspapers and magazines relating to telecom regulation and policy in India. Sridhar has a Ph.D. from the University of Iowa, US, Masters in Industrial Engineering from the National Institute for Training in Industrial Engineering, Mumbai, India and B.E. from the University of Madras, India.

**Vivek Ghosal**

Vivek Ghosal is the Richard and Mary Inman Professor and Director of Graduate Programmes at the Georgia Institute of Technology in Atlanta, US. His current areas of research include: (a) antitrust/competition laws and enforcement, (b) regulatory reform to enhance competition and innovation, and (c) firm strategy related to innovation, M&As, and pricing. Ghosal has published in numerous peer-reviewed journals and has published two edited books ‘The Political Economy of Antitrust’ and ‘Reforming Rules and Regulations: Laws, Institutions and Implementation’. He has been a consultant for international organisations, governments, consulting firms and companies on issues related to antitrust, regulatory reform, business and economic modelling of markets, industry studies, and statistical and econometric modelling.

**Wendy Ng**

Wendy Ng is a Lecturer at Adelaide Law School at the University of Adelaide. She researches in competition law, focussing on China, development, and political economy issues. She obtained her PhD from the University of Melbourne, where her thesis was awarded the Chancellor’s Prize for Excellence in the PhD Thesis and the Harold Luntz Graduate Research Prize for Best PhD Thesis. A book based on her thesis will be published by Cambridge University Press. She is also an editor of the China Competition Bulletin and has been a consultant to the Australian Competition and Consumer Commission. Previously, she was a lawyer at leading law firms in Melbourne and New York.

## Foreword



To make the world a better place to live for all, member States of the United Nations adopted the 2030 Agenda for Sustainable Development in September 2015. This represents a plan of action for people, the planet and for prosperity and is a clear recognition of the need for global strategies to the global problems that we face. Agenda 2030 not only presents us with a set of sustainable development goals but also the necessary means of implementation. In this framework, governments will need to integrate these goals into their policies and laws, and take considered measures towards their achievement.

Throughout this process, UNCTAD will of course act in support and partnership with member States. Through its analytical work and research, UNCTAD aims to inform economic policymakers, helping them in their decision making, and promote policies that optimally address global and domestic economic inequalities and contribute to the 2030 Agenda.

It is widely acknowledged that sustainable and inclusive economic growth requires higher levels of economic productivity through diversification, technological upgrading and innovation. Appropriate industrial and trade policies are necessary but not sufficient to achieve this. There remains a need for complementary and coherent policies that ensure countries benefit from free trade. Competition policy is one of these policies, which governments need to develop and implement in order to achieve the goals of the 2030 Agenda.

One of the fundamental aims of competition policy and law is to increase competitive market pressures by addressing anticompetitive business practices, as well as anticompetitive State regulations and measures. When these pressures are absent, especially due to the presence of monopolies or cartels, then higher prices, lower quality products and economic injustice will prevail. This will have adverse effects for the poorest and most vulnerable people, most especially if those markets are concerned with the provision of basic goods and services.

Effective competition policies may address market failures and create a competitive business environment, thereby promoting efficiency and

stimulating innovation. Such an environment will consequently increase consumer choice and enhance product quality.

Competition regimes could also promote the development agenda by influencing policymaking through advocacy activities. Competition authorities should cooperate with sector regulators and other government bodies to ensure that regulations or policies do not violate competition principles, whilst remaining complete and coherent.

This publication serves to shed light on the role of competition policy and law as essential policy tools towards achieving sustainable and inclusive development. It provides a series of studies, which clearly reflect, from a pragmatic perspective, the importance of effective implementation of competition policies and regulations for sustainable development. Competition and regulatory reforms undertaken throughout the world show the importance of competition not only for economic growth but also for job creation and innovation by small and medium-sized enterprises (SMEs). In countries or sectors where economic power is highly concentrated in the hands of a few corporate groups, competition policy and law may contribute to inclusive growth by promoting the participation of underprivileged economic agents, through the establishment of rules of fair and free competition. This is particularly relevant for entities such as SMEs, smallholder farmers or businesses owned by historically underprivileged populations.

I would like to emphasise the importance of using the framework of competition in regional integration agreements to promote equitable regional arrangements. Appropriate competition policies and laws, as well as their effective implementation, are key to restoring fair competition at a regional level and to maximising the benefits from regional integration agreements in favour of the public interest, rather than particular vested interests.

I would like to thank CUTS for their invaluable work in promoting competition policy for achieving sustainable development, ever since its establishment over 30 years ago. I reiterate that UNCTAD, as it has been for over three decades, is committed to continuing its work in the areas of competition and consumer protection policies, all the while working closely with civil society organisations, such as CUTS International.

**Dr. Mukhisa Kituyi**  
Secretary General  
UNCTAD



## Preface



In September 2015, countries adopted the 2030 Agenda for Sustainable Development along with a set of 17 ‘goals’ referred to as Sustainable Development Goals (SDGs) to end poverty, protect the planet, and ensure prosperity for all. World leaders agreed to develop structured national action plans to achieve these ambitious ‘global goals’ through the participation of both state and non-state actors. The international community made commitments to support such processes and programmes.

CUTS International’s mission of ‘consumer sovereignty in the framework of social justice, economic equality and environmental balance within and across borders’ is well aligned with a number of these SDGs. Hence, CUTS endeavoured to explore how some of its initiatives under specific programmatic areas synergise with some of the SDGs. Pursuant to this ambition, CUTS envisaged this volume entitled, ‘Pursuing Competition and Regulatory Reforms for Achieving Sustainable Development Goals (SDGs)’. Competition Policy and Law is one of the programmatic areas of CUTS, and hence was keen to explore the contribution of competition and regulatory reforms towards achievement of the SDGs.

This publication was made possible by a project that CUTS has been implementing with support from DFID (UK) and BMZ (Germany) facilitated by GIZ (Germany). The project entitled ‘Competition Reforms in Key Markets for Enhancing Social & Economic Welfare in Developing Countries’ (CREW Project, [www.cuts-ccier.org/CREW](http://www.cuts-ccier.org/CREW)) has been implemented in four countries: Ghana, India, The Philippines and Zambia in two sectors: Staple Food and Passenger Transport. The aim of the project is to demonstrate impacts of competition and regulatory reforms on consumer and producer welfare. The experience of the CREW project inspired CUTS to explore the relevance of competition and regulatory reforms for achievement of the SDGs, especially in developing and least developed countries.

There is little disagreement that competition reform is an extremely important component of a market economy. Effective markets are crucial for growth and economic development, especially in the developing ‘south’ and can contribute to job creation and poverty reduction. Anticompetitive policies and practices in the market affects producers and consumers alike – thereby stifling the process of economic growth. It is logical to deduce that there is scope for introduction of elements of competition and regulatory reforms into structures and national action plans to achieve some of the ambitious SDGs.

CUTS and CUTS Institute for Regulation & Competition (CIRC) have designed a unique initiative for the last 10 years, to provide a platform for international practitioners and experts to expand the frontiers on competition and regulatory reforms, thereby contributing to the discourse on competition reforms in the developing world. Once every two years, CUTS and CIRC organises the Biennial Competition, Regulation & Development Forum.

The 4<sup>th</sup> edition of this conference was held in Nairobi in December 2015 with support from DFID (UK), BMZ (Germany) and GIZ (Germany). In addition, the G-77 Secretariat, World Bank and OECD came forward to support this conference, given its focus on “Relevance of Competition & Regulatory Reforms in Pursuing Sustainable Development Goals (SDGs) in Developing Countries”.

The agenda of this conference ([www.cuts-ccier.org/CREW-Final\\_Conference](http://www.cuts-ccier.org/CREW-Final_Conference)), was developed based on the findings of the CREW project – which has boosted CUTS confidence that competition and regulatory reforms can indeed help meet some of the objectives enshrined in the SDGs. In the run up to the conference, CUTS had issued a ‘Call for papers’ for scholars and practitioners from both the developed and the developing world to present their views on four distinct ‘thematic areas’ that would help strengthen the understanding about the interface between competition reforms and the SDGs. These ‘thematic areas’ were:

- (i) Government Policy Promoting Competition, Innovation and Jobs
- (ii) Competition for Inclusive Economic Growth
- (iii) Competition Reforms as a Tool for Public Welfare
- (iv) Trade, Regional Integration and Competition Reforms

This volume presents a set of 16 papers contributed from across the globe from Australia to Argentina – which were carefully selected by a panel of distinguished scholars on the subject. Conscious of the volume of this publication, we have categorised it into four Parts corresponding

with the above four ‘thematic areas’, for easy reading. We hope the readers will find this volume to be an interesting composition of contemporary academic thinking and practice – which would enhance the visibility of competition and regulatory reforms in the context of the achievement of the SDGs.

Finally, I would like to extend my sincere gratitude to my colleagues for timely preparation of this publication. My sincere gratitude to Mukhisa Kituyi, Secretary General of UNCTAD for writing an excellent Foreword, and we thank him for having formally inaugurated the conference in Nairobi. CUTS would like to extend our warm appreciation to all writers who responded to the ‘call for papers’. It was indeed a tough assignment for reviewers to select papers for this publication. We thank our development partners for their support and cooperation in making this volume possible.

**Pradeep S. Mehta**  
Secretary General  
CUTS International



## An Overview

The conference entitled, ‘Relevance of Competition and Regulatory Reforms in Pursuing Sustainable Development Goals (SDGs)’ was organised by CUTS in Nairobi, Kenya on 12-13 December, 2015. This was the culmination event of a three-year project being implemented by CUTS (referred to as the CREW project, [www.cuts-ccier.org/crew](http://www.cuts-ccier.org/crew)) and was designed as the 4<sup>th</sup> CUTS/CIRC Biennial Competition, Regulation & Development Forum. The earlier three forums were held in New Delhi, India.

Being organised close on the heels of the adoption of the ambitious ‘Agenda 2030 for Sustainable Development’, this event aimed to explore the relevance of competition and regulatory reforms as tools for achieving some of these ‘global goals’. The section below tries to highlight this linkage through some illustrations.

### Linking Competition Reforms with SDGs

It was revealed from the discussions in the conference as well that while the link between competition reforms and some of the ‘global goals’ (SDGs) were **direct**, it was rather **indirect/weak** with the others.

#### GOAL 1 (End poverty in all its forms everywhere)

Poverty reduction is one of the steepest challenges for developing country policymakers – hence, remains a priority in government policies. An important approach to **poverty reduction** is to empower the poor, provide them with productive employment and increase their access to land, capital and other productive resources. But this approach may not be successful unless these people are **linked to the markets** and **markets are made to work for the benefit of the poor**.

**GOAL 2 (End hunger, achieve food security and improved nutrition, and promote sustainable agriculture)**

Food is a basic necessity but is prone to **anticompetitive** tendencies, especially affecting its pricing and its availability. How committed are governments to deal with these anticompetitive tendencies in dealing with these problems? In some countries, on average, about 40-45 percent of income is spent on food expenditure and any policy that can be used to make food less expensive would complement poverty reduction efforts.

Effective **agricultural** sector policies, which facilitate greater (and regulated) engagement of private sector in ‘inputs’ markets like fertiliser and seeds, has the potential (as demonstrated under the **CREW and other projects**) to make good quality inputs available at lower costs to farmers, especially benefitting small farmers. In many developing and least developed countries, monopolies (public and private) seem to control **agriculture markets**, which make it difficult for small farmers to derive benefits while selling their produce in these markets.

**GOAL 3 (Ensure healthy lives and promote well-being for all at all ages)**

Based on existing literature and practice, it is now well-established that a healthy competition regime (accompanied with sound regulatory framework) can be instrumental in improving **access to healthcare services and medicines**, especially in developing countries. In most developed countries, various stakeholders in the supply chain are regulated extensively to improve the affordability and availability of medicines as well as maintain levels of service.

**GOAL 4 (Ensure inclusive and equitable quality education and promote life-long learning opportunities for all)****GOAL 5 (Achieve gender equality and empower all women and girls)**

There is growing recognition that public policy in developing world can no longer remain oblivious of the needs and aspirations of women – whether in the social setting or from an economic angle. Governments and development partners are now investing lot of resources and attention to explore avenues for boosting women’s economic empowerment, as a means to strengthening their position in society. CUTS has also noted this from the experience in Ghana, where ‘women traders’ (referred to as ‘Market Queens’) are seen to control over 95 percent of the procurement of staple food (maize) – and are very highly respected.<sup>1</sup>

Similarly, women self-help groups (SHGs) in various parts of India have grown from being a pastime activity to a major contributor of the

village economy in many parts of the country.<sup>2</sup> In both these (above) cases, scope was created in policies to ensure greater participation of women in specific ‘economic’ activities – and should be looked at as lessons for polity.

Existence of various types of barriers and challenges for women to engage meaningfully in various markets is well documented – and is something that governments and development partners need to look closely at.

**GOAL 6 (Ensure availability and sustainable management of water and sanitation for all)**

**GOAL 7 (Ensure access to affordable, reliable, sustainable, and modern energy for all)**

Across the developing world, inefficiency of the public sector as the sole provider of these services in meeting citizens’ demands led to the proliferation of private providers in them. The evolution of the regulatory framework and the policy environment was not able to keep pace with this process, and therefore led to ‘market failures’. Therefore, benefits of economic liberalisation and private sector engagement in these sectors have not led to the envisaged benefits (meeting citizens’ needs). Attainment of these goals would not be possible without the development and application of effective regulatory frameworks in these sectors, which should also encourage ‘citizens engagement’ in these reforms.

**GOAL 8 (Promote sustained, inclusive and sustainable economic growth, full and productive employment and decent work for all)**

**GOAL 9 (Build resilient infrastructure, promote inclusive and sustainable industrialisation and foster innovation)**

There is abundant evidence in literature and practice of how a well-functioning/vibrant market can stimulate innovation, productivity and efficient resources use – key pointers for achievement of inclusive and sustainable economic growth. Dutz and Hayri (2000) established that there is a strong correlation between the effectiveness of competition policy and economic growth. Kahyarara (2004) established a positive relationship between competition policy and productivity, investment and exports.

Further, the volume of infrastructure needs in developing countries imply the engagement of private sector through public procurement processes. Incorporation of ‘pro-competitive’ elements in public

procurement process can help participation of a number of private sector operators in the bidding process, and help save costs.

## Lessons for Policy

The CREW project (Competition Reforms for Enhancing Social & Economic Welfare in Developing Countries) generated knowledge and evidence to reinforce the belief that promoting competition reforms through relevant policies can contribute towards achievement of social and economic welfare. The core objectives of the CREW project were to:

- enhance understanding of the benefits from effectively undertaking competition reforms in developing countries as an intrinsic part of the overall reforms agenda;
- develop and test a methodology (with indicators) for assessing the efficacy of competition reforms in achieving impacts on developing country consumers and producers;
- sustain the momentum on prioritising competition reforms, gained from stakeholder awareness and greater understanding about the associated benefits and participation in related processes in developing countries; and
- advocate for greater importance to competition policy and law issues in the national development agenda to national and international stakeholders.

The following **key policy lessons** emerged from the CREW project, which are relevant for the wider community of policymakers and practitioners – especially in the staple food and bus transport sectors. These issues were discussed in details during the two day event:

- i. There is value in having the right regulatory safeguards (mostly competition policy) in place to ensure that benefits of trade and economic liberalisation can be derived fully by the citizens/country.*
- ii. Although subsidies are generally a departure from normal competition principles, they can assist farmers in remote areas where the private sector might generally not be willing to participate.*
- iii. Government grain procurement institutions might be best suited to focus on maintaining strategic reserves (for food security*



*purposes). Both public and private entities should participate in the procurement process with the overall objective to ensure that procurement is done on time, farmers get the right price for their produce and that payments to farmers are made at the time of transaction.*

- iv. Although keeping public sector run transport companies has helped in ensuring that cheaper transport exists, these are characterised by several inefficiencies. Many governments have maintained 'monopoly' public sector operators in this market, which has imposed considerable financial burden on the government.*
- v. Bus fare regulation process should be done in such a way that there is a balance between enhancing consumer and producer welfare. Right now, in many developing countries, this process is neither scientific nor inclusive or transparent. Given the pressure on urban areas, governments should focus on developing effective regulatory framework for bus transport.*

## Key Take-aways for Practitioners

The discussions during the two day conference were also instrumental in revealing the following key 'take aways' for practitioners of competition policy and law, especially in the developing countries:

### **(i) Continued misgivings about competition benefits by policymakers**

Considerable efforts have been made by advocates and researchers to bring practical evidence based on real examples on the critical role that competition, enhanced by competition reforms, plays in better allocation of resources and higher level of GDP and growth. However, there is still low level of buy-in about the importance of competition reforms by policymakers, particularly in developing countries. This is because some conspiracy theorists are also lobbying against competition reforms, mostly because they benefit from anticompetitive practices.

In addition, although competition reforms help all progressive stakeholders in the growth agenda, promotion of the competition reforms agenda has been left mainly to the competition authorities, with other arms of government taking a back seat, often swayed by the above 'lobbyists'. Critical government arms responsible for policy reforms are therefore vulnerable to lobbying by powerful businesses (often found to

be perpetrators of anticompetitive practices). Competition advocates thus need to ensure that they remain aware of such challenges and devise strategies to adequately articulate the correct position regarding the impact of competition reforms to growth, to enhance buy-in of competition reforms in developing countries.

**(ii) Importance of competition enhancing policy reforms in promoting innovation and jobs**

Based on case studies presented in conference papers from Nigeria, Mexico, China and India, the importance of adopting competition oriented reforms in promoting innovation and jobs was also discussed. From a paper from Nigeria, the impact of having more choice through competition in secondary schools in Nigeria was discussed. It was recommended that policymakers should focus on supply-side reforms that would entail assessment of availability of good quality of schools in the ‘marketplace’. At the same time, educational authorities should also develop indicators of ‘performance measures’ of schools, especially to ensure that there is some level of competition at the time of admission. Lessons from the implementation of competition law in Mexico demonstrate the importance of encouraging competition policy to spread its roots in the domestic system first, before supporting those roots through international assistance. International support without a strong domestic competition system is bound to create limitations in terms of impact on the economy.

In China, the Chinese government and the competition agencies expressly linked competition law and policy with China’s development goals. Thus, since the 2008 Anti-Monopoly Law, much of competition law discourse was focused on the role of competition law in helping to improve people’s wellbeing and livelihood in addition to promoting the pursuit of innovation by businesses. This, therefore, made it easy for government buy-in.

Lessons from India in the staple food sector (wheat) showed that private participation in the seeds sector was picking up in States like Bihar – and the benefits were gradually being felt by the farmers. Although organized agriculture markets were introduced under the Agriculture Produce Market Committees in the 1970s with the objective of protecting farmers from exploitation by intermediaries, the policy denied private investment, invited corruption, and artificially restricted the number of market players, resulting in restrictive and monopolistic markets with high transaction costs.

**(iii) The role of competition in inclusive growth**

Competitive markets tend to impose limitations in promoting innovation, demonstrating the need for a regime that protects intellectual property rights to compliment competition objectives. Competition on its own might discourage innovation, demonstrating the need for significant initiatives, policies and institutions to stimulate innovation in developing economies.

Improperly targeted subsidies also tend to cause market distortions. For example, the Zambia government introduced a floor price at which maize would be procured by the Food Reserve Agency (FRA). This was set above market prices. Contrary to the envisaged impact of benefiting the poor smallholder maize farmers, the high prices benefited only the net maize sellers, comprising only about 28 percent of all farming households. The net sellers are mostly better off farmers who can produce more as poor farmers do not largely sell to the FRA. Thus, improperly targeted subsidies, which are generally a departure from competition principles, tend to distort competition with little benefits to farmers, which does not promote inclusive growth.

**(iv) Competition reforms as a tool for public welfare**

Competition reforms also serve as a tool for enhancing public welfare, which includes both consumer and producer welfare. Although competition is often promoted by enhancing private sector participation, benefits from such competition are often subdued by policy barriers, leaving consumers at the mercy of market distortion effects. Examples include India, where policy measures to promote competitive grain trading were introduced in the 2000s, but continue to be characterised by road-blocks due to administrative instruments and interventionist measures from policy. While competition is not the panacea for public welfare, it complements other tools that can be used to safeguard the interest of both consumers and producers in trade.

**(v) Continuous dialogue between competition advocates and public policy implementers at national level**

As explained in the earlier section, competition and regulatory reforms can be used as a tool to attain certain social and economic objectives aligned with specific SDGs. There seems to be direct interface with SDGs 1, 2 and 3. Further, competition policy can also be seen to be relevant in the attainment of SDGs 4 to 9.

It is, therefore, crucial that a process of continuous dialogue is initiated and sustained between the competition fraternity (and advocates) and government officials, agencies and other practitioners involved with the designing and implementation of programmes for achievement of various SDGs at the national level.

**(vi) Inter-linkages between competition policy, trade and regional integration**

While regional integration brings with it benefits to regional economies, the different levels of development and capacities among member states means that small economies and small firms are usually vulnerable to market dominance by larger firms, who are normally from richer economies. As a result, safeguards are needed in the form of an effective competition law and a sound regulatory environment, which can play an important role in preventing market distortions and ensuring consumer welfare. Where regional integration gives rise to market dominance or market distortion, it results in perpetuation of inequality among and within the integrating countries. Incorporating competition rules and related regulatory reforms into regional trade agreements can therefore strengthen economic growth and market integration. The benefits of incorporating competition rules in regional integration help address barriers within member states' borders, as well as cross-border anticompetitive business practices that cannot be remedied by trade policy instruments.

**(vii) Need to properly package 'benefits of competition'**

In his keynote speech at the conference, the Guest of Honour, Dr. Ekwow Spio-Garbrah, Trade & Industry Minister of Ghana pointed to the need for competition policy advocates to show demonstrable benefits of competition to SMEs and private sector to ensure that they do not oppose competition policy and law. The presence of many banks in Ghana, which can be seen as reflecting high levels of competition, has not necessarily brought about competition as interest rates in Ghana are between 30-100 percent even though there are about 40 banks and over 200 micro finance institutions.

It was also pointed out that business is likely support any policy reform which can be seen to have a positive impact on profit, which is the main motive for business. Thus, the impact of competition reforms on profits needs to be properly explained to business. In addition, competition reforms also mean different things to different people, which is why some stakeholders may not support the process. This generally underlines the

need for creating awareness about what competition is within the context of competition policy and how the benefits are expected to materialise. This is something that the CREW project endeavoured to do – and CUTS would continue to reach-out with its knowledge to people in the developing world.

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## Endnotes

- 1 Refer to the Ghana Diagnostic Country Report (prepared under the CREW project of CUTS) at:  
[http://www.cuts-ccier.org/CREW/pdf/Diagnostic\\_Country\\_Report-Ghana.pdf](http://www.cuts-ccier.org/CREW/pdf/Diagnostic_Country_Report-Ghana.pdf)
- 2 Assessment of success and failure of SHGs in India, available at:  
[http://planningcommission.gov.in/reports/sereport/ser/ser\\_shg3006.pdf](http://planningcommission.gov.in/reports/sereport/ser/ser_shg3006.pdf)



Section I:

# Government Policy Promoting Competition, Innovation & Jobs

Role of Government in promoting sustainable  
economic growth through competition reforms thereby  
creating employment and facilitating innovation





Part I:  
Theoretical Overview



# 1

## Governance Mechanisms and Regulation

### *Test of the Mediating Effects of Regulatory Decision Tools in the Communications Regulator*

KUO-TAI CHENG  
Associate Professor  
Department of Environmental and Cultural Resources,  
Institute for Human Resource Development  
National Hsin-Chu University of Education  
Taipei, Taiwan

#### **Abstract**

Research shows consistent relationships between governance mechanisms and regulations. In this study, the authors developed and tested a model of regulation for examining the mediating effects of regulatory decision tools on the relationships between governance mechanisms and regulations in the communications regulator. Covariance structural analyses revealed regulatory decision tool variables to be influential mechanisms through which governance mechanisms affect regulation. Specifically, regulatory instruments and delegated powers mediate the effects of independence and participation on regulation. Although accountability was related to delegated powers, neither accountability nor personnel was related to enhanced regulations. The importance of the proposed regulatory decision tool model is discussed in this study.

## Introduction

Research related to regulatory governance has recently clarified the utility of using governance mechanisms for enhancing regulation. Such research<sup>1</sup> has demonstrated that governance mechanisms are indeed associated with regulations with some governance mechanisms, such as independence-enhancing regulations are administered across countries while other governance mechanisms are correlated with specific sectors or countries. For example, Stern and Holder used six governance mechanisms – namely, clarity of roles and objectives, autonomy, participation, accountability, transparency, and predictability – to assess 13 Asian developing countries for the Asian Development Bank (ADB)<sup>2</sup>.

Case studies by international organisations, such as the World Bank and ADB offer interesting narrative views but cannot allow statistically robust effects of the relationship and mediation from the development of an independent regulatory agency. Relatively little literature is available on measuring governance mechanisms, regulations, and regulation decision-making tools, where privatisation, liberalisation, and regulatory agencies started<sup>3</sup>.

Furthermore, very little research has examined the mechanisms through which governance mechanisms influence regulations<sup>4</sup>. According to Cheng (2015), results showed that relevant governance mechanisms and regulation predict both individual and organisational capture. Further, regulation partially mediates the relationship between governance mechanisms and regulatory capture in the regulatory space.

The mechanism of ‘accountability’ was found to play a critical role in the prediction of regulatory captures because it had direct impact on individual capture and indirect impact on individual and organisational capture through its relationship to regulation. Further, participation was found to play a critical role in the prediction of organisational capture, and its effect was primarily direct rather than indirect.

Currently, little empirical research exists on governance mechanisms and regulation by the mediating effects of regulatory decision tools. As Majone argued, the international diffusion of regulation as a distinct type of policy making seems to be particularly important in explaining the current renaissance of regulatory analysis<sup>5</sup>.

Furthermore, no attempt has been made to explain the relationship in the extent of regulatory problems and practice. Are regulations, governance mechanisms, and regulatory decision tools linked to the communications regulator and the instruments deployed by the regulator? The purpose of the present study is to build on these findings and enhance understanding

of governance mechanisms by assessing the regulatory decision-making processes that mediate relationships between governance mechanisms and regulations.

The purpose of this paper is to discuss the main issues arising from some recent theoretical literature and its implications for regulatory practice, which will provide the basis for producing the hypotheses. The need exists to explore relevant research linking governance mechanisms, regulation, and regulatory decision tools in order to discuss research pertaining to regulation and governance mechanisms as well as formulate expectations for the relationship between these constructs.

Thus, this study is designed to test the hypotheses. Section 2 summarises the argument about governance mechanisms and regulation and discusses some of the underlying issues affecting the relationship among governance mechanisms, regulation, and regulatory decision tools. Section 3 discusses the research method and scales. Section 4 presents the research analysis and results. The paper ends with a few concluding discussions.

## **Literature Review**

### **Regulation and Governance Mechanisms**

“Like many other political concepts, regulation is hard to define, not least because it means different things to different people.”<sup>6</sup> In the Organisation for Economic Cooperation and Development (OECD)<sup>7</sup> report, regulation refers to the diverse set of policy instruments by which governments set up requirements on enterprises and citizens. Regulations include laws, formal and informal orders, and subordinate rules issued by all levels of governments and rules issued by non-government or self-regulatory bodies to whom governments have delegated regulatory powers.

Regulation, in general, explains the idea of the imposition of controls, restraints, and the application of rules<sup>8</sup>. However, regulation is hard to define as it relies on different explanatory ways. Regulation is “both a technical fix to a problem and a source of problems itself and (...) inherently a site where different political and economic forces come into contest”<sup>9</sup>.

As Black argues, “regulation is the sustained and focussed attempt to alter the behaviour of others according to defined standards or purposes with the intention of producing a broadly identified outcome or outcomes, which might involve mechanisms of standard-setting, information-gathering and behaviour-modification”<sup>10</sup>.

As Black argued that definitions of regulation implicit the term regulatory state even more limited<sup>11</sup>. In this study, ‘Regulation’ is defined as a type of legal instrument and process, and is the control of service providing public utilities as well<sup>12</sup>. Regulations for public utilities are controlling, governing, directing, altering, adjusting with reference to some standard or purpose. Therefore, regulators can have incentives for regulatory failures, and there should be clear governance mechanisms that limit or curb potential misbehaviour.

Furthermore, Levy and Spiller (1994) defined the governance structure as “the mechanisms that societies use to constrain regulatory discretion and to resolve conflicts that arise in relation to these constraints<sup>13</sup>”. Ashworth, Boyne and Walker (2002) argued that, according to the evidence in Wales, regulatory misbehaviour and performance ambiguity are the most noticeable problems and are more prevailing in local services than in national services.

“Apart from the problem of ‘capture’, too much discretion by regulators also increases the ‘regulatory risk’ faced by regulated firms, with potentially adverse effects on regulatory outcomes.”<sup>14</sup>

In practice, it is of significance for regulatory agencies to forfend interpretation of their objectives as well as avoid discretion. Therefore, regulatory governance – firmly grounded in the wider theme of *good governance*<sup>15</sup> also refers to the complexity of the interplay of policy actors in the process of regulation. This suggests the need for regulatory design incorporating governance mechanisms. Thus regulatory governance mechanisms should be designed to limit regulatory failures.

“Regulatory mechanisms should therefore be designed to limit regulatory risk. For example, statutory or legal requirements on the regulators to ensure that firms can finance their regulated activities can reduce the risk of regulatory expropriation and avoid a possible source of investment distortions, thereby increasing social welfare<sup>16</sup>”.

Moreover, tensions between different levels of regulatory governance appear in practice, indicating the need for a combined regulatory governance of the effects of the different governance mechanism on regulatory performance<sup>17</sup>. As such, it can be argued that strong and effective governance features (including sound decision-making processes) are essential as the only way discovered thus for offering boundaries and accountability on regulatory decisions.

Regulatory processes can be thought of as a design mechanism with two dimensions<sup>18</sup>: governance and incentives. Regulatory governance entails the creation of a transparent and predictable regulatory system that can be sustained over time<sup>19</sup>.

Regulatory incentives refer to the mechanisms that are connected with pricing, subsidies, and other operating policies. Regulatory governance initially matters more than regulatory incentives as the sustainability of the institutional environment reform is developed primarily and initially from a sound and strong framework of regulatory governance<sup>20</sup>.

In addition, in the absence of either a regulatory agency or any prior experience in regulating public and private utilities sectors, it is reasonable to assume that a sound and strong framework of regulatory governance initially represents a commitment by the government to reduce regulatory failure<sup>21</sup>.

Gulen, Makaryan, Volkov, and Foss (2007) offered a list of governance mechanisms that different studies found to be desirable or even necessary. They then determined four most important government mechanisms: Independence, Enforcement Powers, or Authority, Transparency and Accountability, and Competency.

According to their analysis, transparency and accountability appear to be unanimously desired characteristics. Some studies<sup>22</sup> even offered further governance mechanisms, such as Communication, Consultation, Consistency, Predictability, Impartiality, and Flexibility that put into transparency and enhance accountability.

In 1997, the UK Better Regulation Task Force (BRTF) published its Principles for Good Regulation, defining five principles: transparency, accountability, proportionality, consistency, and targeting<sup>23</sup>.

These principles are very similar to those in Smith's<sup>24</sup> study. Meanwhile, Stern and Holder (1999) used six governance criteria for the ADB: clarity of roles and objectives, autonomy, participation, accountability, transparency, and predictability. All of these authors emphasised on the clarity of assignment of functions, regulatory autonomy, accountability, and transparency.

Further, for the regulatory body to realise its role as effectively as possible, the regulation seeker's coverage of the regulator, the jurisdictional boundaries between the regulatory body and the Ministry, and relations with other regulators are of interest<sup>25</sup>. It is also evident that the regulatory agency should not be influenced by the regulation seeker's subject to its regulation.

Warrick Smith (1997) argued the importance of independence, defining it with following requirements:

- Distant relationship with the regulatees, consumers and other private interests;
- Distant relationship with political authorities

- attributes of organisational autonomy, such as earmarked funding and exemption from restrictive civil service salary rules – necessary to further the growth of the requisite expertise and corroborate those having not so close relationships.

However, Levy and Spiller (1996) do not make substantive suggestions about the required nature of governance mechanisms other than to emphasise the need to correspond to the institutional endowment of the countries in question. “Regulators have the power to generate and redistribute rents across various interest groups, for instance, by creating or preserving monopoly positions or by maintaining cross-subsidies in the tariff structure”.

Therefore, they might have incentives to use this power to gain or maintain support from their political principals. “At the same time, regulated firms or the beneficiaries of regulation, such as user groups have a strong incentive to attempt to ‘capture’ the regulator. There is also a risk that the regulators will use their discretion to expropriate producers, distorting investment incentives in the industry. These political economy considerations point to the need for careful design of regulatory frameworks<sup>26</sup>”.

Therefore, the need exists to set up governance mechanisms to restrain the discretionary scope of regulators and resolve the conflicts between regulators and those seeking regulation.

The contemporary literature identifies four possible approaches: economic, social, political, and institutional. Cheng and Hebenton (2008) argued that only the institutional approach is quite robust to investigate regulation and governance. Such an approach also provides the advantage in that it allows for the exploration of the five interrelated aspects (clarity of roles; participation; independence; accountability and transparency) of a regulatory framework that captures the main governance mode of regulation and governance. These formed the basis of the questionnaire used in the current study<sup>27</sup>.

An OECD report, Gonenc *et al.* (2000) highlighted the need to design regulatory governance mechanisms and institutions to abridge the possibility of regulatory capture by regulation seeker or other interest groups as well as the effects of regulatory uncertainties on the regulation seeker’s investment behaviour<sup>28</sup>. On the other hand, Correa *et al.*<sup>29</sup> argued that “independence and accountability attributes are more developed than regulatory means and instruments, mostly qualified personnel and regulatory tools and decision-making procedures, particularly with respect



to those mechanisms that can guarantee consistency of decisions and reduce arbitrariness”.

Most of these variables of governance mechanisms for regulation have been analysed in studies of governance and regulatory governance conducted by, for instance, the World Bank, OECD, ADB, National Economic Research Associates (NERA), International Monetary Fund (IMF), and many researchers. Levy and Spiller<sup>30</sup> argued that “the governance structure incorporates the mechanisms a society uses to restrain the discretionary scope of regulators and to resolve the conflicts to which these restrain give rise”.

It is also necessary and of significance to determine to which extent particular solutions to the challenges of regulation and governance are embedded in traditions and practices specific to national political and administrative systems and probably also to particular policy fields<sup>31</sup>.

Cheng and Hebenton (2008) conducted a qualitative analysis on governance mechanisms for telecommunication liberalisation and regulation. Their results showed that governance mechanisms are important in the process of liberalisation and regulation. In addition, liberalisation can generate very few welfare improvements when not combined with good regulatory governance and robust legal framework.

However, their results do not show the relationship between governance mechanisms and regulations. Thus, we expect that each of the five governance mechanisms (clarity of Roles, Accountability, Transparency, Participation, and Independence) in the current study will have significant correlations with regulations.

### **Regulatory Decision Tools**

Regulatory decision-making processes range from formal hearings, as in the United States, to more informal processes, such as those in the United Kingdom. Wherever the balance is struck, the focus should be on transparency in decision-making, which reduces opportunities for improper influences and underscores the fairness and legitimacy of decisions<sup>32</sup>.

According to Smith’s work, regulatory decision-making process usually enhances governance mechanisms that can extend regulation seeker interested in a decision with the opportunity to express their views, release the decision and the elaborate reasons for concluding that decision, and challenge the decision through an appeals process to assure that the regulatory body remains accountable.

In Correa *et al.*'s (2006) survey, 18 of the 21 agencies surveyed were legally required to formally document the decision-making process, detailing the actions of each actor involved. However, only eight regulators were required to cite jurisprudence in support of their decisions, weakening the consistency of regulatory decision-making over time.

In addition, formal documentation of the decision-making process was legally required and must contain every legal action of those actors directly involved in the process. Also important was the fact that in the case of only six regulators, decisions were made without previous communication and discussion among board members<sup>33</sup>.

Therefore, the regulatory agency is a non-departmental public organisation mainly involved with rule making, which might also be responsible for face finding, monitoring, adjudication, and enforcement<sup>34</sup> (Levi-Faur, 2011). Regulatory agencies have become highly popular by delegating powers from the government to independent regulatory bodies, thereby enabling the executive to reassure regulation seekers that it will not be able to arbitrarily intervene in the market.

Furthermore, the degree of delegation involves the level to which the executive, the legislature, or both seek to bind their hands in order to produce credibility and predictability<sup>35</sup>. However, appropriate legal delegation is clearly not enough to secure effective regulation<sup>36</sup>. The content of regulatory decision-making is important, but the key issue is the decision tools if the objective is to guarantee regulatory credibility and stability.

The survey of Brazil regulatory agencies stated that five out of the eight regulatory instruments presented. For example, methodology for tariff revision and instruments for quality monitoring were available for at least 13 agencies. More sophisticated instruments, especially those related to economic regulation (as opposed to technical regulation), were less available. Almost all surveyed agencies considered themselves to have the power and legal means to secure compliance with their decisions.

However, one-fifth of the agencies' personnel was admitted by public examinations (this share was higher for older agencies than for the newer ones), with this share being 26 percent and 18 percent among federal and state agencies, respectively. Approximately, 95 percent of the agencies' staff had undertaken short-term courses<sup>37</sup>.

Independence refers to governance mechanisms that isolate regulatory body from the interests of the regulatee. As regulatees assess the regulatory decision-making process, both the decision-making rules and participation facets should be well-considered. An additional important mechanism is

accountability, which refers to offering effective arrangements for appealing the regulatory agency's decision.

To strengthen the regulatory decision-making process, transparency is needed to ensure open decision-making that necessitates publishing decisions and meetings by unwrapping relevant information, declaring in advance the schedule of meetings and their respective agendas, and making available to third parties the minutes of meetings held<sup>38</sup>.

In other words, regulators require not only the right to ask information, but also the substantive legal powers and regulatory instruments to enforce the request (for example, issue warnings and impose fines). The quality of selection of personnel is also significant in the regulatory decision-making process.

Earlier discussions of regulation and governance have emphasised a number of GMs, such as the agency's autonomy and the clarity of its roles and objectives; decision-making processes, transparency, and predictability; decision tools and personnel; and participation and accountability. Other mechanisms to describe regulatory governance have also been suggested in the literature<sup>39</sup> suggested five critical mechanisms:

1. Accountability
2. Independence
3. Clarity of roles
4. Participation and
5. Transparency

In this study, we opted to test Reg, GMs, and regulatory decision tools (RDTs), which are closely linked in the literature.

As Minogue asserted (2002), "to understand fully the 'governance of regulation'... we must also examine the characteristics of the public policy process. This means looking beyond the institutional façade to grasp the 'real world' of public action"<sup>40</sup>. Regulations, as institutions, establish rules for agents and create structures of incentives and constraints<sup>41</sup>.

In addition, both formal and informal institutions and their enforcement qualities are fundamental, and enforcement depends heavily on informal rules, such as norms, customs, and conventions<sup>42</sup>. The institutional approach adopted in the research is the study of institutions, described by Rhodes<sup>43</sup> as 'a subject in search of a rationale'. It is also "a subject matter covering the rules, procedures, and formal organisations of government"<sup>44</sup>.

However, institutions are no longer equated with organisations (Lowndes, 2002, p.91). Rather an "institution is understood more broadly

to refer to a stable, recurring pattern of behaviour”<sup>45</sup>. In other words, the institutional approach highlights formal regulations and organisational structures and behaviours as well as informal conventions<sup>46</sup> that add breadth and depth to an understanding of institutional links in the regulatory decision-making.

Regulatory decision tools that help review the regulation are a key way to improve the quality of the regulation. Improving regulatory quality is an ongoing task that is becoming important in the regulatory policy agendas in Taiwan. Consequently, communications regulations need to be framed within the context of governance, not government. Communications regulation in this research is firmly grounded in the broader theme of good governance.

Further, it is involved in exercising regulatory functions that go beyond the design and implementation of regulatory decision tools, or their coordination, and also embrace wider issues that are integral to governance mechanisms, such as clarity of roles, participation, independence, accountability, and transparency. Regulatory governance also refers to encompassing the complex interplay of regulators, governance mechanisms, and their decision tools in the process of communications regulation. Therefore, the institutional links for decision tools and governance mechanisms for regulations are critical for ensuring that objectives are achieved; otherwise, there is a risk of policy or regulatory failure.

Finally, it can be argued that there is a need to explore relevant research linking governance mechanisms, regulations, and Regulatory Decision Tools (RDTs) to discuss research pertaining to regulations and governance mechanisms as well as formulate the expectations for the relationships between these constructs. In the following chapter, the study designed to test hypothesised model will be described, which is as following:

- Hypothesis 1: Regulatory instruments correspond with regulation.
- Hypothesis 2: Delegated powers and regulations exhibit a positive, direct relationship.
- Hypothesis 3: The positive relationship between delegated powers and regulations is mediated by regulatory instruments.
- Hypothesis 4: Regulators scoring high on accountability report stronger intentions regarding personnel of regulatory decision tools.
- Hypothesis 5: Regulators scoring high on independence report stronger intentions regarding regulatory instruments of regulatory decision tools.

Hypothesis 6: Intentions for regulatory instruments mediate a positive relationship between independence and regulation.

Hypothesis 7: Regulators scoring high on participation report stronger intentions regarding delegated powers of regulatory decision tools.

Hypothesis 8: Intentions for delegated powers mediate a positive relationship between participation and regulation.

## **Method**

### **Participants and Procedure**

Mounting pressures to ensure better regulations are also arising from communications development in Taiwan. Regulation has moved into many new areas, while the complexity of rules has also increased. Regulatory processes encompass the development of new regulations, the revision of existing regulations, and the implementation of existing regulations.

A range of regulatory decision tools and governance mechanisms have been developed to improve the outcomes of regulatory processes. These trends indicate that regulatory governance for a communications regulatory agency is more crucial than ever. One of the central goals of communications regulators is to ensure that regulations efficiently produce economic, social, and administrative benefits, i. e. that benefits justify costs that costs are the minimum needed to produce any level of benefits, and that resources are allocated to their highest values.

Hence, it is important for communications regulators to understand the likely consequences of different regulatory decision tools and governance mechanisms and to compare them with the goals of economic, social, and administrative regulations.

The participants comprised 164 employees in the National Communications Commission (NCC), an independent regulator of Taiwan. The response rate was 82 percent. There were 49 women (30 percent) and 115 men (70 percent). The mean level of job experience was 29.45 months ( $SD=30.17$  months). Data were obtained during a concurrent test validation project.

Prior to testing, all participants were given a letter containing a brief explanation of the purpose of the study (i.e., test validation) and a research statement ensuring the confidentiality of their individual test results. Immediately after testing, participants completed a regulatory decision tools questionnaire, which was short demographic form requesting background information.

One important element of this research is the analysis of the effect of regulatory governance in the communications. In fact, there is a need for the research on the links among regulation, governance mechanisms, and regulatory decision tools to help regulators have a better understanding of the regulatory policies for which they are responsible or to which they may make a contribution.

Grindle (1980) argued that, in order to understand reform elements, the behaviour of regulators and constraints on their actions must be studied against the backdrop of the institutional contexts within which they operate. This opens a space for choice in the design and implementation of regulation and decision tools by considering factors that influence these regulatory choices and actions. As a result, the contributions of regulatory officers are significant to regulatory governance in communications regulatory decision-making.

For the purposes of the studies envisaged under this research, regulatory officers were selected to obtain focussed results and avoid the constraints of data sources. The decision of whom to select was made using multiple criteria, so that representation is possible across a number of facets of governance for regulation.

Information from regulatory officers is highly valued as they are the regulators who have the most knowledge regarding institutional links for regulatory decision tools and governance mechanisms for regulation. Informants were more articulate, more knowledgeable, and closer to the event, action, process, or setting than others. One of the advantages of this approach is the ability to investigate a contemporary phenomenon, such as regulatory decision tools, governance mechanisms, and regulatory governance within a real-life context.

### **Measures**

The study adopted a cross-sectional approach to measure all variables simultaneously. An anti-common method variance (CMV) strategy was also embedded in the measurement. A series of standardised scales were used, as detailed in the sub-sections.

### **Governance Mechanisms**

Governance mechanisms were adopted to measure governance mechanisms for regulation. This scale is composed of 25 items<sup>47</sup>. Sample items included:

- How would you evaluate the interference from other government authorities to the practices of regulatory agency?

- How would you evaluate the influences from the regulated utility to the practices of regulatory agency?
- How would you evaluate the current information collecting mechanism of regulatory agency?
- How would you evaluate the importance of collecting opinions from the regulatees, consumers and other stakeholders in the regulatory decision-making?
- How would you evaluate the importance of legal requirements for the publication of the regulatory agency's decision?

The participants' responses were recorded using a 5-point Likert scale (1=completely disagree, 5=completely agree). Higher scores meant higher levels of governance mechanisms, indicating that participants demonstrated more governance mechanisms for regulation<sup>48</sup>.

### Regulation

The regulation scale was based on the definitions of OECD (1997) and Black (2002). This scale is composed of nine items. Three kinds of regulations – 'economic', 'social', and 'administrative' – were used to measure the outcome of regulation, as perceived by the respondents, who were employees of a regulatory agency.

Sample items included '*Is regulation useful to do the price regulation?*' and '*Is regulation useful to reduce the paperwork?*'

The participants' responses were recorded using a 5-point Likert scale (1= completely disagree, 5 = completely agree). Higher scores meant a higher level of expectation, indicating that participants had stronger expectations toward regulation<sup>49</sup>.

### Regulatory decision tools

The regulatory decision tools scale was revised and used to measure regulatory governance in infrastructure industries<sup>50</sup>. The regulatory decision tools scale is a nine-item measure. Sample items included '*How do you evaluate regulatory instruments are available to the operation of regulatory agency?*', '*How do you evaluate regulatory instruments are available the agency's power to promote competition in the market?*', and '*How would you evaluate the human resources and expertise available to the agency?*'

The responses were based on a 5-point Likert scale (1 = completely disagree, 5 = completely agree). Higher scores meant a higher level of expectation, indicating that participants had stronger expectation toward using regulatory decision tools.

## Results

Table 1.1 presents correlation coefficients and other descriptive statistics for all variables assessed in this study. Relationships between GMs and RDTs are generally as predicted: The largest correlation for accountability is with personnel ( $r=0.15$ ), independence is with regulatory instruments ( $r=0.48$ ), and participation is with delegated powers ( $r=0.39$ ). Participation is also correlated with regulatory instruments ( $r=0.39$ ).

Furthermore, the GMs expected to correspond with regulation are indeed correlated with regulators' ratings ( $r=0.21$  and  $0.26$  for independence and participation, respectively).

Finally, as expected, regulatory instruments and delegated powers are correlated with regulation ( $r=0.36$  and  $0.21$ , respectively), whereas personnel is not significantly related to regulation ( $r=-0.10$ ). Taken together, the correlational results support many of the hypotheses postulated in this study and prompted an examination of the relationships among these variables using the maximum-likelihood method of covariance structure analysis to test for mediation (Bentler, 1995).

**Table 1.1: Descriptive Statistics and Inter-correlations among All Variables**

	M	SD	1	2	3	4	5	6	7	8	9
1. Independence	103.8	14.9	(0.89)								
2. Clarity of Role	86.7	18.4	0.41*	(0.84)							
3. Participation	107.5	13.5	0.47*	0.34*	(0.84)						
4. Accountability	97.3	12.5	-0.23*	-0.18*	-0.01	(0.83)					
5. Transparency	95.8	16.1	0.36*	0.20*	0.21*	-0.03	(0.91)				
6. Personnel	28.3	5.2	0.04	-0.11	0.01	0.15†	0.09	(0.76)			
7. Regulatory Instrument	43.3	7.6	0.48*	0.18*	0.39*	-0.11	0.12	0.14†	(0.89)		
8. Delegated Powers	46.9	5.5	0.32*	0.15†	0.39*	0.10	0.09	0.08	0.50*	(0.88)	
9. Regulation	35.9	12.8	0.21*	0.14†	0.26*	-0.12	-0.05	-0.10	0.36*	0.21*	(0.86)

*Note: Reliabilities are reported in parentheses along the diagonal. The 95 percent confidence interval for correlations greater than or equal to 0.16 does not include 0 ( $0.01 < 0.16 < 0.31$ ). The 90 percent confidence interval for correlations greater than or equal to 0.14 does not include 0 ( $0.01 < 0.14 < 0.27$ ).*

a  $N = 164$ .

\*  $p < 0.05$ , two-tailed. †  $p < 0.05$ , one-tailed.



To ameliorate the effects of common-method variance (CMV) resulting from the utilisation of self-rated measures, the authors collected the data in two stages. CMV emerges when self-rated measures are simultaneously used, as in some cases the observed relationships between variables are inflated, jeopardising the reliability of data analysis<sup>51</sup>.

To assess the potential for regression coefficient instability, collinearity diagnostics were conducted. Specifically, we calculated variance inflation factor (VIF) scores, which measure the extent to which collinearity among the predictors affects the precision of a regression model in each step. Variance inflation is the consequence of multicollinearity. VIF scores of less than 10 are typically considered acceptable<sup>52</sup>. No VIF score exceeded 1.9. Harman's single factor test has been adopted to examine the potential CMV<sup>53</sup>.

All the research variables were first merged into one factor, and the results showed poor fit, suggesting that one single factor of merging all variables was inappropriate for the data analysis ( $\chi^2(210) = 3664.32$ ,  $p < 0.001$ ,  $\text{RMSA} = 0.15$ ,  $\text{NFI} = 0.45$ ,  $\text{CFI} = 0.19$ ,  $\text{IFI} = 0.21$ ,  $\text{SRMR} = 0.16$ ). Then an unmeasured latent construct method to measure the potential influence of CMV is adopted as recommended by Podsakoff *et al.* (2003).

The chi-square difference test was not statistically significant [ $\Delta\chi^2(1) = 3.60$ , *ns*]. Results were consistent with the findings of Harman's single factor test. To simplify, the influence of CMV was very less; hence, the research dataset should be accepted for further data analysis.

The first three hypotheses, concerning relationships among the regulatory decision tools variables and regulation, were specifically tested with comparisons of three substantive models.

First, a saturated model (Model 1) was tested that included all hypothesised paths between the governance mechanisms variables and mediator variables, direct paths from independence and participation to regulation, paths from regulatory instruments and delegated powers to regulation, and paths from delegated powers to regulatory instruments and personnel.

Second, a model was tested that eliminated the path between delegated powers and regulatory instruments (Model 2). Third, a model was tested that retained the delegated powers-regulatory instruments path but eliminated the delegated powers-regulation path (Model 3). The results of these analyses, as well as additional models described below, are shown in Table 1.2.

**Table 1.2: Fit Indices for Covariance Structure Analysis**

Model Number and Type	x2	df	CFI	NFI	RMSEA	Model comparison test		
						Compa- rison	$\Delta x^2$	df
1. Saturated model	25.29	17	0.97	0.91	0.05			
2. Without delegated powers – regulatory instruments path	56.45	18	0.84	0.79	0.11	2 vs.1	31.16*	1
3. Without delegated powers – regulation path	25.42	18	0.97	0.91	0.05	3 vs.1	0.13	1
4. Direct effects only <sup>a</sup>	83.06	20	0.73	0.70	0.14	4 vs.3	57.46*	2
5. Indirect effects only <sup>b</sup>	27.90	20	0.97	0.90	0.05	3 vs.1	2.48	2
<p><i>Note: N = 164 for all chi-square analyses. CFI = comparative fit index; NFI = normed fit index (any goodness of fit &gt; 0.90 is an indication of acceptable overall model fit); RMSEA = root-mean-square error of approximation (any RMSEA &lt; 0.10 is an indication of acceptable fit).</i></p> <p><sup>a</sup> <i>With direct effects on Reg only. This model does not include paths from GMs to the RDT variables.</i></p> <p><sup>b</sup> <i>With indirect effects for GMs only. This model does not include direct effects from governance mechanisms to regulation, although there are direct effects from the RDT variables to regulation. Thus, this model represents the hypothesised mediation model.</i></p> <p><sup>*</sup> <i>p &lt; 0.05, two-tailed.</i></p>								

Models 2 and 3 are both nested within Model 1, allowing the use of chi-square difference tests to compare models. A comparison of the saturated model (Model 1) and the model leaving out the delegated powers-regulatory instruments link (Model 2) yielded a significant result,  $\Delta x^2$  (1, N=164) = 31.16,  $p < 0.01$ , supporting at least partial mediation of the delegated powers-Reg relationship.

A comparison of Model 1 with the model leaving out the delegated powers-regulation link (Model 3) yielded an insignificant result,  $\Delta x^2$  (1, N =164)=0.13, ns, supporting the complete mediation of the delegated powers-regulation relationship by regulatory instruments.

Thus, Hypothesis 3 is supported over Hypothesis 2, as the relationship between delegated powers and Reg is not direct, but rather completely mediated by regulatory instruments. Hypothesis 1 is also supported by a significant relationship ( $\beta = 0.41$ ,  $p < 0.01$ ) between regulatory instruments and regulation.

Hypotheses related to the GMs variables were similarly tested with a series of comparisons whereby Model 3 was compared with two additional nested models. The first additional model (Model 4), the direct-effects-

only model, eliminated the independence-regulatory instruments and participation-delegated powers paths. The second additional model (Model 5), the indirect-effects-only model, retained the GMs-mediator paths but eliminated the direct effects from independence and participation to regulation.

A comparison of Model 3 and Model 4 yielded a significant result,  $\Delta x^2(2, N=164) = 57.64, p < 0.01$ , suggesting that the effects of independence and participation on regulation are at least partially mediated by the regulatory decision tools variables. A comparison of Model 3 and Model 5 yielded an insignificant result,  $\Delta x^2(2, N=164) = 2.48, ns$ , suggesting that the regulatory decision tools variables mediate the effects of independence and participation on regulation.

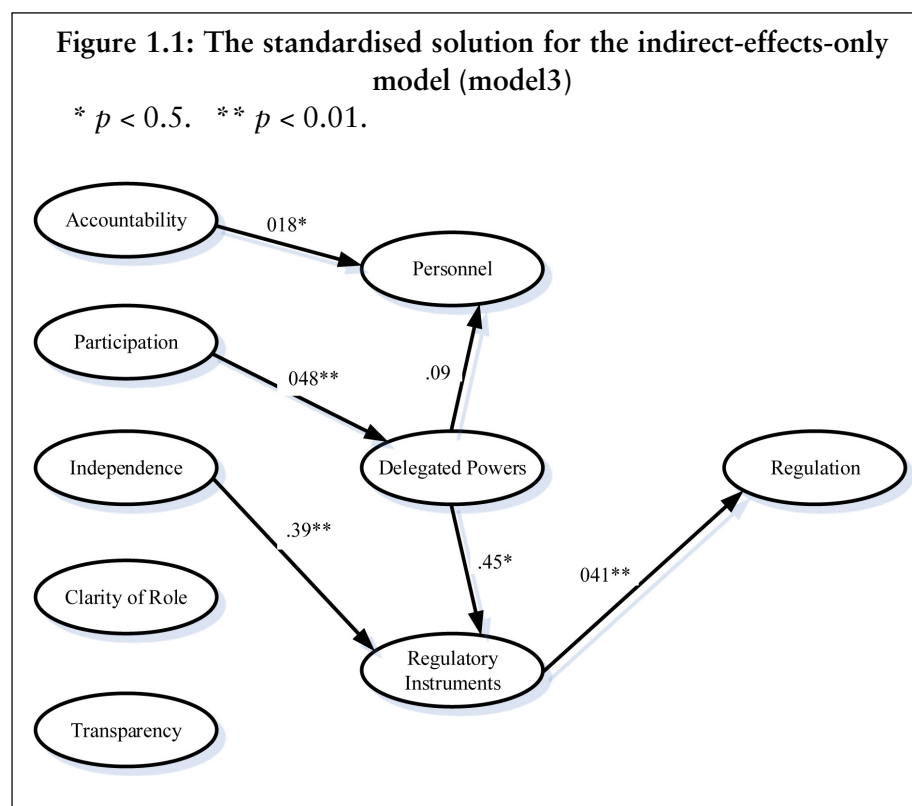
The hypothesised model of mediation (Model 5, the indirect-effects-only model) thus fit the data acceptably:  $x^2(20, N=164) = 27.90$ , comparative fit index = 0.97, normed fit index = 0.90, root-mean-square error of approximation = 0.05. The standardised solution for this model is presented in Figure 1. Hypothesis 4 is supported by the significant linkage between accountability and personnel ( $\beta = 0.18, p < 0.05$ ).

Hypothesis 5 is supported by the significant relationship between independence and regulatory instruments ( $\beta = 0.39, p < 0.01$ ). Hypothesis 6, predicting regulatory instruments to mediate the independence-Reg relationship, is supported by finding the hypothesised mediation model (Model 5) to have a fit equivalent to the fit of the model that also included a direct path between independence and regulation (Model 3). The independence-regulation relationship is approximately 76 percent mediated by regulatory instruments.

Hypothesis 7 is supported by the link between participation and delegated powers ( $\beta = 0.48, p < 0.01$ ). Hypothesis 8, predicting that delegated powers mediate the participation-Reg relationship, is supported by finding the hypothesised mediation model (Model 5) to have a fit equivalent to the fit of the model. This also included a direct path between participation and regulation (Model 3).

To further explore the nature of the effect for participation, we examined whether the association between participation and regulation was also mediated directly through regulatory instruments. To test this finding, we examined an additional model that added a path between participation and regulatory instruments to the model reported in Figure 1.1. The fit indices did not improve, suggesting no direct relationship between participation and regulatory instruments.

This test suggests that a direct path between participation and regulatory instruments is not an alternative to the mediated relationship through delegated powers. The overall indices, along with the nested model comparison tests, thus indicate that the theoretical model of mediation (Model 5) fits the data well. The participation-regulation relationship is approximately 35 percent mediated by delegated powers and regulatory instruments.



## Discussion and Conclusions

Relatively little is known about the mechanisms through which governance mechanisms affect regulation. Limited research<sup>54</sup> has provided initial support for the long-held view related to the proximal means by which GMs affect Reg through regulatory decision-making process.

This study extends the knowledge of this relationship by focussing on three fundamental regulatory decision tools that regulators can pursue in

the regulatory process, including personnel. For example, the regulator's employee is admitted by public examinations), delegated powers. For example, the regulator has sufficient legal powers and means to secure compliance with its decision, and regulatory instruments (the regulator has the power and legal means to guarantee compliance with its decision).

Hypothesis 1 is supported by a significant relationship ( $\beta=0.41, p<0.01$ ) between regulatory instruments and Reg. Hypothesis 3 is also supported over Hypothesis 2, as the relationship between delegated powers and Reg is not direct, but rather completely mediated by regulatory instruments. Moreover, Hypothesis 4 is supported by the significant linkage between accountability and personnel ( $\beta=0.18, p < 0.05$ ). Hypothesis 5 is supported by the significant relationship between independence and regulatory instruments ( $\beta = 0.39, p < 0.01$ ).

The results demonstrate that regulatory instruments and delegated powers (indirectly through regulatory instruments) mediate relationships between two governance mechanisms (participation and independence) and regulation. Independent regulators were more likely to be enhanced by regulatory instruments, which in turn enabled them to perform better as regulators. Participation was more likely to enhance delegated powers, which linked to regulation through regulatory instruments. Mediation for the independence – regulation relationship is relatively easy to interpret. The major portion of the relationship between independence and regulation was indirect through regulatory instruments, as expected.

The nature of mediation for the participation – regulation relationship is somewhat weaker and more complex. The indirect effect of participation on regulatory instruments is mediated through delegated powers. Nevertheless, a moderate direct effect also remained between participation and regulation.

Hypothesis 6, which predicted that regulatory instruments mediate the independence-regulation relationship, is supported by the finding that the hypothesised mediation model (Model 5) has a fit equivalent to the fit of the model that also included a direct path between independence and regulation (Model 3). Hypothesis 7 is supported by the link between participation and delegated powers ( $\hat{\alpha} = 0.48, p < 0.01$ ).

Hypothesis 8, predicting that delegated powers mediate the participation-regulation relationship, is supported by the finding that the hypothesised mediation model (Model 5) has a fit equivalent to the fit of the model that also included a direct path between participation and regulation (Model 3).

Our results suggest that regulatory instruments, rather than delegated powers, are the enhanced decision tool most strongly associated with regulation. Nevertheless, the evidence suggests that delegated powers should be retained in models explaining how governance mechanisms and affect regulation.

First, modest correlations with regulatory instruments and with personnel suggest that delegated powers are indeed a separate construct. Second, the post hoc analyses related to participation illustrate that the effect of participation on regulatory instruments is mediated by delegated powers. For these reasons, it is believed that it is significant for future research to examine all three regulatory decision tool variables, not just personnel and regulatory instruments.

The personnel factor was positively related to accountability, as expected. This finding supports the hypothesis that highly accountable regulators are more likely to be enhanced to get along with other regulatees in the regulatory process, although the personnel factor for regulatory decision tools was not related to regulation in the NCC.

Therefore, we are unable to test all dimensions of the proposed decision tools model within the context of the present study, and any conclusions related to personnel are tenuous and incomplete. Future research should examine whether a path between delegated powers and personnel explains regulation in the NCC, in which there is greater opportunity for the personnel of regulatory decision tools. It should also be noted that accountability, clarity of role, and transparency were not found to be strongly related to regulation.

Although our literature findings support the utility of a model based on the five governance mechanisms and regulations, we acknowledge that other perspectives of GMs exist, such as predictability<sup>55</sup>. Other perspectives focus on differences, such as regulatory capacity<sup>56</sup> and autonomy<sup>57</sup>. Still other perspectives focus more on context factors such as institutional endowment<sup>58</sup>.

Additional research is needed to integrate these concepts within our model. Moreover, the support for the regulatory decision tool perspective that we adopt should not necessarily be interpreted as evidence against other perspectives that similarly help us understand the complex regulatory process. A potential limitation of this study is that both the GMs and RDTs measures were obtained from self-responses, thereby introducing common-method bias.

Due to the fact that intentions are virtually impossible to measure except through self-response, future studies might try to reduce this confound by

obtaining alternative indicators of governance mechanisms. Nevertheless, given the governance mechanisms – RDT correlations obtained in this study (mean  $r=0.18$ ; maximum  $r=0.48$ ), it seems reasonable to conclude that our measures of governance mechanisms and RDT are likely assessing separate constructs. A second limitation of this study is the cross-sectional design, which does not allow for an assessment of causality.

Thus, for example, we are unable to definitively test the validity of the assumption that delegated powers cause regulatory instruments. An alternative explanation is that regulators are enhanced to attain regulatory instruments in order to have more delegated powers.

Overall, the present study extends current theory in two primary ways. First, it provides support for a process model of regulatory decision tools that combines governance mechanisms and RDT variables. Such findings enhance our understanding of how governance mechanisms affect regulation. These findings also underscore the central role of the regulator in determining regulations in the regulatory process. Second, our study supports and extends the development of theoretical models of regulation.

Regulatory decision tools have long been viewed as having a central role in regulation. This study adopts the decision-making perspective and identifies broad decision tools toward three fundamental orientations in the regulatory process: personnel (for example, the regulator's employee is admitted by public exams), regulatory instruments (for instance, the regulator has the power and legal means to guarantee compliance with its decision), and delegated powers. For example, the regulator has sufficient legal powers and means to secure compliance with its decision).

Although the relative importance of these regulatory decision tools might differ depending on the demands of specific sectors and countries, the proposed framework appears to comprehensively specify a decision tool, explaining what regulators are trying to decide in the regulatory process – namely, personnel, delegated powers, and regulatory instruments. Assessing a regulator's decision through these three broad tools provides one method for comprehensively measuring regulatory decision-making in the regulatory process.

Future models investigating the determinants of regulation might thus benefit from including measures of personnel, delegated powers, and regulatory instruments as tools of decision-making.

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## Endnotes

- 1 Gutierrez & Berg, 2000; Minogue, 2002; Stern & Holder, 1999; Xia, 2012a
- 2 *Ibid*
- 3 Minogue, 2002
- 4 Vining & Weimer, 1999
- 5 Majone, 1999, p. 309
- 6 Levi-Faur, 2012, p. 3
- 7 1997b, p. 6
- 8 Foster, 1992; Koppel, 1999
- 9 Baldwin, Cave, & Lodge, 2010, p. 4
- 10 Black, 2002, p. 26
- 11 Black, 2002, p. 11
- 12 public utilities as well (Bauer, 2005; Cook & Minogue, 2002; Florio & Fecher, 2002; OECD, 1997a, 2002
- 13 p. 205
- 14 Gonenc, Maher, & Nicoletti, 2000, p. 44
- 15 Cheng & Hebenton, 2008; Chou & Liu, 2006; Stern & Holder, 1999; Xia, 2012b
- 16 Gonenc *et al.*, 2000, p. 45
- 17 Isopi, Nosenzo, & Starmer, 2014; May & Winter, 1999; Verhoest, Peters, Bouckaert, & Verschuere, 2004
- 18 Levy & Spiller, 1996
- 19 *Ibid*
- 20 Al-Kassab, Ouertani, Schiuma, & Neely, 2014; Campell, 1996; Gutierrez & Berg, 2000; Lombardi, Trequattrini, & Battista, 2014; Philipson, 1992; Ramaseshan, Achuthan, & Collinson, 2008; Ruys, 1997; Singh, 2000; Xavier, 2000
- 21 Gutierrez, 2003
- 22 Berg, 2000; Gutierrez, 2003; Gutierrez & Berg, 2000; Stern & Holder, 1999
- 23 Better Regulation Task Force, 1997
- 24 W. Smith, 1997
- 25 Cheng, 2007; Gulen *et al.*, 2007
- 26 Gonenc *et al.*, 2000, p. 41
- 27 Cheng & Hebenton, 2008
- 28 Cheng, 2015
- 29 2006, p. 38
- 30 1996, p. 4
- 31 Christensen, 2012
- 32 *cf* W. Smith, 1997



- 33 Correa, Melo, Mueller, & Pereira, 2008; Correa et al., 2006
- 34 Levi-Faur, 2011
- 35 Correa *et al.*, 2006; Levy & Spiller, 1996
- 36 Cheng, 2007
- 37 Correa *et al.*, 2006
- 38 *Ibid*
- 39 Stern & Cubbin, (2005), Cheng and Hebenton 2008
- 40 (p. 658)
- 41 Ogus, 2001, 2002
- 42 North, 1990
- 43 (1995, p.55)
- 44 Rhodes, 1997, p.68
- 45 Goodin, 1996, p.22
- 46 Xia, 2012b
- 47 Cheng & Hebenton, 2008
- 48 Cheng, 2013
- 49 *Ibid*
- 50 Correa *et al.*, 2006
- 51 Podsakoff, MacKenzie, Lee, & Podsakoff, 2003
- 52 Hair, Anderson, Tatham, & Black, 1998; Hair, Black, Babin, Anderson, & Tatham, 2006
- 53 Jakobsen & Jensen, 2015; Podsakoff et al., 2003
- 54 Cheng, 2015; Cheng & Hebenton, 2008; Stern, 2007; Stern & Holder, 1999
- 55 For example, Kessides, 2003; Stern, 2007
- 56 P Smith, 1997; W. Smith, 1997
- 57 Stern & Holder, 1999
- 58 Levy & Spiller, 1996

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# 2

## Role of Government, Sustainable Economic Growth and Competition Reforms

### *An Indian Perspective*

S CHAKRAVARTHY  
*Civil Servant by Profession in India  
Adviser/Consultant on Competition  
India*

#### Abstract

Competition has not been at the heart of the process of policymaking debates in many countries. Its role in economic development, competitiveness of national economies, trade and investment has not been fully appreciated, particularly in developing countries and remains fragile in the political context and in public opinion. Governments over time have adopted trade and regulatory policies in open contradiction with competition principles.

This paper addresses the role of the government towards laying down policies keeping in mind the crucial need for competition to inform them (policies) with a view to sub-serving **sustainable economic growth**.

There is and can be no perfect competition in the real world. What one notices in the market is a set of imperfectly competitive markets, where firms engage in strategic behaviour to maximise their profits and to restrict opportunities available to their competitors. Such kind of behaviour results in the distortion of competition, exploitation of consumers and imposition of various economic and social costs on the society, adversely affecting its welfare in general.

## **Competition and Economic Development**

Market economies are about competitiveness, performance and efficiency and cannot function without competitive conduct of market operators. It is true that markets are shaped by a multitude of other factors including **governmental policies** but without a minimum amount of economic freedom and a culture of competition, the economy is likely to be dominated by rent seeking of operators and prevalence of anti-competitive practices.

This is why the famous Washington consensus of the United Nations of 1989 declared that development would result from trade liberalisation, privatisation and deregulation. Liberalisation can be circumvented by private restraints and the privatisation of public monopolies is likely to miss its target if substituted by private market dominance and collusive practices.

It cannot be gainsaid that competition is essential for achieving the benefits of market liberalisation and competitiveness. This has been recognised by the Monterrey consensus of 2002, which stressed on the importance of private sector development but also the need for good governance in both the public and private sectors.<sup>1</sup> The idea of competition is fundamental to modern economic thinking and there is a well-developed body of theory to explain how the pursuit of economic self-interest, within an appropriate framework, has beneficial effect for economic efficiency, consumers and society.<sup>2</sup>

Economic reforms including competition reforms that disregard market functioning and fail to promote competitive behaviour are bound to fail in their very objectives.<sup>3</sup>

## **Role of Government**

For addressing the role of the government, a distinction needs to be drawn between 'competition law' and 'competition policy'. Competition policy is defined as 'those government measures that directly affect the behaviour of enterprises and the structure of industry'.<sup>4</sup> The objective of competition policy is to promote efficiency and maximise welfare.

There are two elements of such a policy. The first involves putting in place a set of policies that enhance competition in local and national markets. These would include a liberalised trade policy, relaxed foreign investment and ownership requirements and economic deregulation. The second is legislation designed to prevent anticompetitive business practices and unnecessary government intervention – competition law. An effective



competition policy promotes the creation of a business environment which improves static and dynamic efficiencies and leads to efficient resource allocation, and in which the abuse of market power is prevented mainly through competition.

Competition policy can be regarded as a genus, of which competition law is a specie. The former covers a whole array of executive policies and even approaches, whereas the latter is a piece of legislative enactment having the character of enforceability in a court of law.

Government's role combines its responsibility to put in place an appropriate competition law and complement it with its responsibility to posit a well-designed competition policy.

## Multiple Objectives and Conflict

A source of tension in many countries, particularly the developing ones, is the priority attached to competition policy relative to the rank order assigned to other governmental policies, including that having the support of statutes. Multiple objectives are allowed to rein in the competition policy, as a result of which, conflicts and inconsistent results surface to the detriment of the consumers. For instance, promoting small businesses and maintaining employment could conflict with attaining economic efficiency. With this kind of small business objective, competitors rather than competition may get protected.

Competition policy or competition regime seeks to maintain and encourage the competitive process with a view to promoting economic efficiency and consumer welfare. Its objective is to spur firms and individual players in the market to compete with each other to secure the patronage of customers in terms of, *inter alia*, competitive prices, good quality and greater choice for them.

The most common objectives of competition policy applied with varying emphasis in different countries are economic efficiency, consumer welfare and public interest. In his analysis of new concepts for competition policy and economic development, Singh<sup>5</sup> has suggested that standard objectives of competition regime should be reconsidered to bring in notions, such as, *inter alia*, an optimal degree of competition as opposed to maximum competition, an optimal combination of competition and cooperation between firms, dynamic rather than static efficiency and consistency between competition and industrial policies. The role of the Government would therefore, *inter alia*, include framing of a competition policy besides legislating an appropriate competition law keeping in view the goals and needs of the country.

The central exercise therefore, is, to pursue an appropriate competition policy without being constrained by or conflicting with other public policy objectives. Within this exercise, the main issue is the priority attached to competition policy objectives in the overall framework of governmental policies. For this purpose, it is necessary to list governmental policies that impact on competition policy. Micro-industrial governmental policies that may support or adversely impinge on the application of competition policy would include:

- Industrial policy
- Reservations for the small scale industrial sector
- Privatisation and regulatory reforms
- Trade policy
- Procurement policy
- Fiscal Policy

There are more policy areas but only six of them have been chosen because of space restraint.

A National Competition Policy (NCP) would help to address numerous policy-induced competition distortions which otherwise could not be checked under the competition law, because they were sanctioned under other public policies.

**Taking India as an illustration cubicle**, a brief treatment of the six policy areas is attempted below.

## **Industrial Policy**

The Indian statute, Industries (Development and Regulation) Act, 1951 (IDR Act) is essentially designed to promote and regulate industrial development. If competition principles, fair and free trade and market driven environment are desirable objectives, the need for the regulatory statute for industrial development may not be necessary at all. No licence or permission need be a requirement for an industrial undertaking to be set up or for the expansion of an existing undertaking except for location (avoidance of urban-centric location), for environment protection (anti-pollution, banning chemical industries in habitat concentrations), for prevention of use of scarce resources (timber from trees), for discouraging conspicuous consumption, for protection of monuments and National heritage and for protecting the society from threats to public health (tobacco, liquor etc.). Subject to the aforesaid safeguards and similar ones in National interest, the IDR Act doesn't seem to have relevance anymore.

But yet, the IDR Act was used to regulate growth of Industrial activity till 1991, when economic reforms were ushered in. Along with the now repealed Monopolies and Restrictive Trade Practices Act, 1969 (MRTP ACT), the surveillance over Industrial growth was intense. Big becoming bigger was an ugly concept. After the reforms of 1991, many controls called the licence-permit Raj were taken off the Statutes and Regulations. MRTP Act was replaced in 2002 by the new Competition Law, Competition Act, 2002. Many industries were deregulated and no licence is required for them now.

Ironically, MRTP Act, competition law for India from 1969 till 2002 concentrated in regulating, if not inhibiting Industrial growth and in controlling monopolies but hardly fostering competition in the market. Industrial growth is a major source of stability in an economy. The primary objectives of the Industrial policy are to maintain a sustained growth in productivity, to enhance gainful employment, to encourage innovation, to achieve optimal utilisation of human resources, to attain international competitiveness and to transform India into a major partner and player in the global arena.

The signal reform of 1991 focussed on deregulating Indian industry, allowing the industry freedom and flexibility in responding to market forces and providing a policy regime that facilitated and fostered growth of Indian industry. Another reform of great significance was, as mentioned above, the replacement of the MRTP Act by Competition Act, 2002. The Mantra in the new competition law was COMPETITION. Noteworthy is the fact that India has grown significantly industrially over the two decades since the reforms and in particular, competition reforms.

The role of the government needs to focus not only in promoting competition, thereby facilitating growth of Indian industry but to ensure that its policy decisions do not create anticompetitive outcomes. An example of such policy induced distortions is given below:

#### ***Fleet and Equity Requirements for Domestic Passenger Air Service<sup>6</sup>***

According to India's Civil Aviation Requirement (CAR), Section 3, Part II and III, a scheduled service operator using aircraft with a take-off mass of 40,000 kg or more must purchase or lease a minimum of five aircraft with start-up equity requirement of Rs.50 crores. Additionally, as an airline's fleet grows in increments of upto five planes, equity requirements grow by Rs.20 crores. For aircraft with take-off mass less than 40,000 kg, the minimum start-up fleet is five aircraft (purchased or leased) with the minimum equity requirement starting at Rs.20 crores and growing by Rs.10 crores with every five additional aircraft.

Given the high cost of entry into the civil aviation sector, these regulations unnecessarily raise barriers to entry. Hence, the fleet and equity requirement instituted by these regulations limit the number of new entrants.

On the contrary, the incumbent firms are not facing any potential threats from new entrants and hence are following collusive practice amongst them. Without many new competitors entering the market, there exists no incentive to change the way these established airlines operate and therefore, customer service and choice are adversely affected.<sup>7</sup>

## **Reservations for Small Scale Industrial Sector**

India has been following a policy for decades encouraging and protecting the small scale industrial sector. There are both efficient and inefficient small scale units and well-managed and ill-managed ones. Competition principles would dictate the theory that inefficient and ill-managed firms should exit from the market. The concern implicit in this theory is that exit of such firms will render employed persons being thrown out of employment, thus aggravating the unemployment situation in the country. It cannot be denied that the small scale sector generates significant employment but it does so at a considerable cost to the exchequer by way of loss of revenue entailed by a plethora of exemptions from indirect taxes available to this sector of the economy.

Thus, while a policy for the welfare of the small scale sector cannot be regarded as unreasonable, it must be tempered by the knowledge that it involves heavy costs. Reservation of products for small scale and micro enterprises has led to poor quality of output. Since, many of them are suppliers of ancillaries to organised producers, it leads to the overall poor quality of products to consumers. Efficiency of such suppliers is poor because of the lack of skills, low capital availability, poor quality of machinery, heavy labour orientation, poor cost control, low output and poor quality of outputs.

In a paper presented to the Expert Group<sup>8</sup> constituted by the Ministry of Commerce, Government of India to study the interaction between Trade and Competition Policy, a pointed reference was made to the plethora of laws and rules in India that explicitly protect favoured players and reduce competition in the name of public interest.<sup>9</sup>

Public interest is frequently and unabashedly invoked to protect one specific interest group (unionised labour, small scale industries, handloom weavers) with no explanation of how or why the interest of this group transcends all others. Such protectionism in the name of public interest

leads to sacrifice of efficiency, raises potential costs and risks and discourages new investment.

The Expert Group referred to above observed that “all governmental policies will have to be viewed through the competition lens to ensure that consumer interest and welfare and economic efficiencies and development dimensions are not pejorated”.<sup>10</sup>

The trend in the policies of the government, over the years has been towards dereservation of many products, which hitherto have been reserved for the small scale sector. Exempting small scale industries from the applicability of competition law may not be and will not be necessarily a solution for the welfare and interest of the small scale sector. Protection of such units can only be a drag on the economy and waste of scarce resources (particularly capital resources). If at all there should be a national goal in this area, it should be the welfare of the efficient and well-managed small scale sector. Exemption from the competition principles cannot be a handmaiden to be used for protecting laggards in the small scale sector.

Having said this, in order to encourage and assist the efficient and well-managed small scale sector units, policies providing cheap credit to them, increasing the threshold limit for the small scale sector (having regard to inflation over the last few years and the exchange rate changes) and the like could be laid down.

In respect of the small scale sector in India, economic reforms over the last two decades have effected progressive reduction of reservation of products, thus encouraging them to become competitive. The reforms in this area inherit the competition principle.

## **Privatisation and Regulatory Reforms**

Recent years have seen widespread regulatory reforms and the privatisation of many State-owned enterprises in many countries. These reforms have been undertaken as a result of an increased awareness and evidence of regulatory failure. The increase in reliance on market mechanisms to promote economic progress is exemplified by the trend towards the privatisation, de-regulation, adoption and enforcement of Competition Law.<sup>11</sup>

India is now taking on hand the implementing of the second generation economic reforms (the first generation reforms have been under implementation for some time now, particularly after 1991). But still, even now, there are price controls and dual pricing in India leading to distortions in the market. For instance, restrictions on sugarcane prices and procurement, production capacities, dual pricing of sugar (levy and

non-levy), restraint of exports and imports and many others like restrictions have enabled the inefficient producers of sugar to continue and prevent the rise of a competitive industry.

Policymakers in India are aware that there is an imperative need to further the economic reforms of liberalisation, de-regulation and privatisation so as to enable the consumers to reap the benefits of competition in the market. Nonetheless, a caveat needs to be added that while competition principles may govern and inform most governmental policies, there should be some flexibility in the competition policy to provide for the needs, aspirations and goals of the country. It also needs to be said that economic reforms including liberalisation, de-regulation and privatisation should be so designed that they strengthen the competition policy and vice-versa. These two paradigms should be complementary to each other.

## **Trade Policy**

Trade liberalisation and competition reforms are complementary to each other and neither can fully achieve its objects without the other. Given this premise, an appropriate approach would be to adopt competition policy simultaneously with trade liberalisation and other economic reforms such as privatisation and deregulation. In this way, competition policy would act as a catalyst for economic reforms and development based on market-oriented principles.

While an open trade policy will be supportive of competition policy objectives, it is not always that the former will be a guarantor of competition in all circumstances. Governmental policies, particularly those that give rise to restraints and distortions in trade practices and the market, may be a threat to the attainment of competition objectives. All trade policies may, therefore, be required to fall within the framework of competition principles. The framework needs to be based on two parameters, one, whether a restriction affects all competitors or just foreign competitors and the other, whether the restriction falls within the category of measures that have been traditionally subject to competition law disciplines.

Trade policies laid down by the government include measures relating to industrial policies, domestic regulations, licencing requirements, discriminatory standard-setting practices, state monopolies and state trading enterprises, all of which may be restricting competition domestically and impeding market access to foreigners. In the interest of consumers and free and fair trade, it is necessary to have an effective

competition policy to ensure that trade policies fall within the contours of competition principles.

Trade policy includes tariffs, quotas, subsidies, anti-dumping actions, domestic content regulations and export restraints. Trade policies of this kind and of a similar nature need to conform to competition principles and where they do not, will be required to be refashioned, so that they do. To make the competition policy effective it should be ensured that there should be no physical or fiscal barriers to domestic trade from one end of the country to another. It would mean fiscal measures, such as uniform Sales Tax, abolition of Octroi, elimination of such other State level entry or exit taxes and elimination of all physical control of goods movement throughout the country.

The benefits of trade liberalisation have been seen in the relaxation of quantitative restrictions and reduction of tariffs. Yet, the trade policies adopted in furtherance of developmental objectives may have several anticompetitive dimensions. Some likely instances of potential distortions of this nature are given below:

#### *Inverted duty structure*

One of the unusual facets of the current import duty structure is its inverted nature witnessed in a few sectors at present. An inverted duty structure refers to a situation where the duty on the finished product is lower than that on raw materials and intermediate products. This is a distortion when the higher duty on raw materials results in production costs that are higher than the selling price of the imported finished product and hurts the domestic manufacturer who relies on the raw materials for production.<sup>12</sup>

#### *Yet another instance of inverted import duty structure*

A concern rose in the cement industry which, in early 2010, urged the Centre to abolish import duty on raw materials such as coal, petroleum coke and gypsum since cement as a finished product does not attract duty. The industry, therefore, argued that duty on them should be abolished in line with the established principle that import duty on inputs should not be higher than that of finished product. The government was requested to align value-added tax on cement with that of steel at four percent against 12 percent levied currently since both are important raw commodities for the infrastructure sector.<sup>13</sup>

***Safeguard duty***

In July 2010, the Government of India imposed 16 percent safeguard duty on soda ash imports from China in order to protect domestic producers. The safeguard duty was expected to benefit domestic manufacturers of soda ash. However, the market players reported neither increase in the price of soda ash as a resulting impact of such a move nor a reduction in imports from China. According to market estimates India's soda ash imports surged by 69 percent after the safeguard duty imposition.<sup>14</sup>

Even though the collected facts and estimates may lean towards the justification of the imposition of the safeguard duty, thorough investigation needs to be conducted to ensure that the situation merits the levy. Furthermore, a long time span of imposition of the safeguard levy would promote inefficiency among protected domestic producers to the detriment of competition. Levy of safeguard duty can be justified if absence of such duty is seen as associated with a significantly reduced market share of domestic producers, thus, threatening their businesses.

However, as mentioned earlier, care must be taken that the domestic producers do not get too comfortable under this cushion that it becomes a resting spot for inefficiency. The role of the government is manifest in such cases that it should reckon the competition principles before deciding on the imposition of safeguard duty.

**Procurement Policy**

There are many procurement policies that favour some specific companies over others or distort competitive neutrality between the public and private market players by way of some preference clauses, riders or conditionalities or produce anticompetitive outcomes because of the manner in which they may be implemented. While there may be sound policy reasons for these, the benefits need to be compared with the potentially higher prices that distort competition as well as harm the consumers. Hence, it must be established clearly and in a transparent manner that the objectives behind such policies override possible adverse impact on competition and are necessary to achieve some social and environmental objectives<sup>15</sup>. An example is given herein:

In a recent tender call for Ayurvedic medicines, the Directorate of Ayurveda, Government of Rajasthan was seen to bend the rules governing the procurement of medicines by adding riders/conditions that manufacturers must have minimum five years of experience, a condition



that did not figure in the original call for tenders. This condition was inserted later while the tender process was on.

Of the existing PSUs and co-ops that manufacture Ayurvedic medicines, only eight had an experience of five years and more. That an experience of minimum of five years was necessary to ensure the level of quality sought was not adequately demonstrated by the purchase committee and consequently, such a rider acted as a deterrent for entry. Also, operations of most of the qualifying companies were being managed by the same set of people which raised doubts regarding collusive behaviour between the officials and the specific manufacturers.”<sup>16</sup>

### *Purchase preference*

An example of anticompetitive policy of the government is the fact that public sector undertakings (PSUs) are in significant force in India and receive preferences that restrict competition by the private sector. Preference in procurement policies distorts competitive neutrality in the market place. As CUTS research report<sup>17</sup> notes, “[T]he concept of competitive neutrality means that government-supported business activities should not enjoy net competitive advantages over their private sector competitors.”

For some years, PSUs enjoyed purchase preference, if the price quoted by them fell within 10 percent of the lowest bidder’s quote. Wiser counsel prevailed and government did away with the said preference to PSUs in 2008.

## **Fiscal Policy**

Fiscal policy includes, tax policy, expenditure policy, subsidy or state aid, investment or disinvestment strategies and debt or surplus management. Under the existing tax policy, the present multiple tax structure impels high compliance cost, excessive litigation and uncertainty about ultimate tax incidence at the time of investment or business transactions. The competitiveness of the Indian industries is adversely affected by the cascading effect of multi-layered taxes which increases the cost of indigenous manufacture. The inefficiency of the existing indirect tax structure and consequent adverse impact on India’s economic growth are described below:

### *Impact on competitiveness of indigenous goods and services<sup>18</sup>*

The existing tax structure is having a cascading impact on cost of indigenous manufacture of goods and services. For example, value added

tax (VAT) is levied on the sale value of a product which includes excise duty element, Thus VAT is also charged on excise duty amount. Similarly when VAT paid raw material is used in manufacture, it forms part of the excisable value (cost of manufacture) on which excise duty is levied. Thus excise duty is also charged on VAT element.

Similar is a case of service tax levied on services. Central sales tax is levied on inter-state sale of goods. This cascading of taxes at each stage in a supply chain makes Indian goods expensive. In the case of some indigenous products, the resultant competitive disadvantage due to cascading taxes alone can be as high as 10 percent to 15 percent of the price. Such tax disadvantage reduces the competitiveness of indigenous goods and does not allow India to tap the export potential of manufactured goods and agro-based processed foods.

### ***Subsidies/State Aid***

Subsidies have often been used to foster the development of new industries especially in developing countries. Subsidies are also often granted as part of a 'defensive' industrial policy, when they are targeted towards distressed firms, with the goal of preventing foreign takeover, avoiding the disappearance of an activity deemed essential for the country's economy, or avoiding layoffs and the ensuing social troubles.<sup>19</sup>

In India, subsidies are granted both by the Central Government and state governments. Examples include the recurring support to agriculture, power, airlines, and coal mining. Subsidies increase inefficiencies and lead to soft budget constraints for the beneficiary. Governments think that production itself creates economic value-an idea that sometimes makes them protect businesses regardless of their performance. Rampant and wasteful subsidies cause a drain on the fiscal budget as well. An instance is given herein:

In India, agricultural trade policy is a part of a larger food and agriculture policy regime that seeks to maintain food self-sufficiency while providing support to the agricultural sector. The Government of India uses a variety of policy instruments in attempting to achieve these goals, input subsidies being one such major tool. Over the years, the amount of such subsidies has increased to unsustainable levels especially in the fertiliser sector. This has had several detrimental effects where the beneficial effects of such subsidies have been outweighed by macro-economic imbalances.

The huge subsidies granted to the fertiliser industry carry the objective of promotion of domestic agricultural production and achieving self-

sufficiency in food production. This is having an adverse impact on the fiscal deficit. While domestic policy support should continue, the Indian fertiliser industry should be made more competitive in order to achieve efficiency gains in the long run so that gradually such subsidies may be phased out.<sup>20</sup>

## Competition, Economic Growth, Innovation and Efficiency

It cannot be gainsaid that economic growth manifested by increases in employment and real wages is a function of competition in the market. Competition is likely to result in overall enhanced gross domestic product (GDP) growth as well as social gains in terms of greater consumer welfare and over-all poverty reduction. It is, therefore, important that competition is not hampered or distorted by governmental policies.

There is empirical evidence of the benefits of competition policies *vis-a-vis* economic development, greater efficiency in international trade and consumer welfare listed in a Report.<sup>21</sup> The evidence, albeit referring to experiences of developed countries, indicates substantial benefits from the strengthening of the application of competition policy principles in terms of 'greater production, allocative and dynamic efficiency, welfare and growth.'

The Report further concludes that the consumer and producer welfare and economic growth and competitiveness in International Trade have all flowed out of competition policies, deregulation and surveillance over restrictive business and trade practices. Noting that competition rewards good performance, encourages entrepreneurial activity, catalyses entry of new firms, promotes greater efficiency on the part of enterprises, reduces cost of production, improves competitiveness of enterprises and sanctions poor performance by producers, the empirical evidence in the Report suggests that competition ensures product quality, cheaper prices and passing on of cost savings to consumers.

The Report also observes that competition promotes two types of efficiencies namely static efficiency (optimum utilisation of existing resources at least cost) and dynamic efficiency (optimal introduction of new products, more efficient production processes and superior organisational structures over time). The UNCTAD Report provides the following empirical evidence to substantiate its conclusions.

In the Netherlands, it has been calculated that the average annual consumer loss arising from collusive practices or restrictive regulations

in several service sectors amounts to 4,330-5,430 million guilders (around US\$ 2.1-2.7bn).<sup>22</sup> Data relating to the US show that a bid-rigging conspiracy (which was eventually prosecuted) for the sale of frozen seafood had an average mark-up over the competitive price over a one year period of 23 percent.<sup>23</sup> The break down of price-fixing conspiracies in some industries led to steep declines in manufacturing costs.<sup>24</sup>

In a study, Bayoumi et al,<sup>25</sup> have estimated that differences in levels of competition account for more than 50 percent of the current gap in GDP per capita between the Euro area and the US. They conclude that more intense product market competition would enhance growth and employment. Aghion et al<sup>26</sup> and Dutz and Hayri<sup>27</sup> echo these views through their empirical work.<sup>28</sup>

A study<sup>29</sup> by the Australian Productivity Commission, undertaken to assess the benefits of promoting competition in Australia, estimated the expected benefits from a package of competition promoting and deregulatory reforms (including improvements in the competition rules) to lead to an annual gain in real GDP of about 5.5 percent, or A\$23bn, where consumers would gain by almost A\$9bn besides seeing increases in real wages, employment and government revenue.<sup>30</sup>

Innovation increases dynamic efficiency through technological improvements of production processes and/or the creation of new products. Competition, an important driver of productivity spurs innovation, sub-serving the interests of consumers.

Effective competition is the instrument for attaining economic growth through enhanced innovation, efficiency and productivity as well as ensuring social gains by overall poverty reduction and greater consumer welfare. It is therefore of paramount importance that the government consciously formulates policies that are compatible with competition principles. Equally imperative is the need for such policies to promote competition in the market. It has been highlighted *supra* in this paper that competition is often distorted by factors such as anti-competitive practices of enterprises as well as policies and regulations adopted and implemented by the government that have anticompetitive outcomes.

There does not appear to exist any mechanism or a comprehensive policy in the existing competition regime of India which ensures that policies are formulated in a manner that their anti-competitive outcomes are minimised as a result of which, they are least competition restrictive. The extant competition law, Competition Act, 2002 empowers the Competition Commission of India (CCI) to deal with anticompetitive practices such as cartels, price-fixing etc. which cause appreciable adverse effect or have the potential to cause appreciable adverse effect on

competition in the relevant market. But there is no comprehensive policy in force to prevent and avoid distortions induced by Government policies, statutes and regulations. It is understood that a draft NCP has been drafted that is awaiting the approval of the government.

NCP may likely help harmonise government policies and regulations at all levels, foster competitive neutrality and launch competition assessment mechanism for government policies and regulations as well as ensure that deviations from competition principles to serve social and environmental objectives are notified and publicly justified. Finally, such effort needs to be backed by a strong culture of competition and political will in order to be successful in its endeavour.

## Role of Governance

It is in this context that government has the responsibility to inhere good, efficient and effective governance. Most, if not all activities ultimately have at their consummating point, the consumer. Consumer welfare and interest aim at the charter of economic liberty designed for preserving free and unaffected competition as the rule of governance. The premises on which the charter rests are unrestrained interaction of competitive forces, maximum material progress through rational allocation of economic resources, availability of goods and services of acceptable and good quality at reasonable prices and finally a just and fair deal to the consumers. State governance has to factor these, if it has to live up to its responsibilities by the country and its subjects.

*Good governance essentially involves a reform process, which includes fostering of competition in the market.*

Good State governance is likely to serve the interests of consumers and the society, if competition principles inform its myriad policies. *Market* paradigm, if properly implemented has to focus on competition principles, which should inform legislative and executive policies. For buttressing domestic competition, every country needs to have a sound competition policy and an appropriate competition law to enforce the policy. Competition reforms are the need of the hour.

Competition reforms would help in travelling towards the broad objectives outlined above by focussing on the following:

1. All policies of the government need to be cleared on the touchstone of *Competition*
2. Using the provision relating to advocacy in Competition Act, 2002 (section 49), the existing policies of the government may be examined

and tested on the touchstone of competition and amended as may be appropriate

3. Governmental policies and regulations need to be harmonised in terms of competition principles
4. Competitive neutrality between public and private market players should be ensured
5. Any deviation from competition principles should be notified with justifications, as for instance, on social and environmental objectives
6. The NCP should be finalised expeditiously and brought into force
7. Political will as necessary to implement competition reforms needs to be nursed
8. Effective steps towards creating *competition culture* in the country need to be undertaken

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# 3

## Competition Advocacy as an Anti-Rent-Seeking Policy

### *An Empirical Analysis*

TIM BÜTHE

*Associate Professor, Political Science and Public Policy  
& Senior Fellow for Rethinking Regulation  
Kenan Institute for Ethics, Duke University, USA*

RACHEL GLANZ

*Student, Department of Political Science, Duke University, USA*

#### **Abstract**

The rapid adoption of competition regimes across the developing world in the last 25 years<sup>1</sup> suggests a growing consensus that economic development and prosperity is predicated on competitive interactions among producers. Much of the early work on how to achieve the full benefits of a competition regime in developing countries focussed on the specificity and breadth of prohibitions of anticompetitive behaviour encompassed in a country's competition *laws*, the strength of the enforcement of such prohibitions, and whether or not competition laws in developing countries should include merger regulation. By contrast, both academic research and practitioners' initiatives by the International Competition Network (ICN), the World Bank (WB), the Organisation for Economic Cooperation and Development (OECD), and others have increasingly emphasised on the importance of a broader competition policy, and in particular the centrality of competition advocacy.

Competition advocacy has been defined by the ICN as the “promotion of a competitive environment for economic activities by means of non-

enforcement mechanisms, mainly through [a competition agency's] relationship with other governmental entities and by increasing public awareness [of] the benefits of competition."<sup>2</sup> For developing countries with relatively 'young' competition agencies, a growing literature recommends a focus on competition advocacy as a way to achieve significant gains at relatively modest expense and as a chance to both gather expertise and build political support.

A key objective of such an advocacy role for competition agencies is to establish *within the government* a vocal promoter of competition principles, as a counterweight against rent-seeking by private actors through anticompetitive laws or regulations (or against ministries/agencies with particularistic agendas). As the ICN put it: "By having a competition advocacy role, the agency can counter or at least minimise the adverse effects of rent-seeking behavior prevalent in [many] countries."<sup>3</sup>

But can competition advocacy by public competition agencies yield the promised benefits? Does it? There is a striking dearth of empirical work examining whether — and, if so, under what conditions — competition advocacy by competition agencies indeed serves the public interest. In this paper, we provide what we believe is the first systematic empirical analysis using data from outside the US to examine competition advocacy as an anti-rent-seeking policy.

We are able to do so because the World Bank (WB), from 2002-2005, included in its enterprise surveys in some countries questions that asked about political lobbying by the respondents' own company or in their industry. The responses to these survey questions, which focused specifically on lobbying legislators and government officials for laws and regulations that would yield material benefits for the company, provide an exceptionally direct measure of the level of rent-seeking activity, allowing us to analyse the effectiveness of competition advocacy as an anti-rent-seeking policy in Ukraine.

The selection of Ukraine for a case study of competition advocacy as an anti-rent-seeking policy may seem surprising, given the political upheaval in Ukraine since the 2013-14 revolution and the problems with which the Ukrainian competition agency has struggled in the aftermath, including being implicated in corruption scandals disclosed after the 2014 regime change.<sup>4</sup>

For analytical purposes, however, an examination of competition advocacy in Ukraine 2002-2005, is not just unencumbered by the later problems of the Ukrainian competition regime, it holds exceptional analytical promise: Ukraine is one of the few countries in which the rent-seeking questions were asked on two WB Enterprise Surveys (in 2002

and 2005), and it is the only one that experienced – between the first and the second WB survey – a significant competition law revision that strengthened the advocacy powers of the Ukrainian competition agency.

We show that the increased advocacy role for the Ukrainian Antimonopoly Committee (AMC) indeed resulted in a substantial, statistically highly significant decline in the level of rent-seeking, which does not appear to be explicable by specific events or broader developments in Ukraine's sometime turbulent political economy. The findings suggest that forceful competition advocacy holds great promise for reducing rent-seeking and thus fostering sustainable development.

## **Competition Advocacy: Foundations for a Theory**

In a significant shift, competition advocacy has recently become popular among scholars and competition policy practitioners alike. In the 1990s, when competition policy experts from Latin America started to call for greater emphasis on competition advocacy in the work of developing country agencies, many competition law experts in OECD countries were still skeptical. These experts considered advocacy at best a questionable distraction from the law enforcement task and an undesirable diversion of scarce agency resources — and at worst a dangerous politicisation of the work of competition agencies.<sup>5</sup>

Today, competition policy scholars widely consider advocacy the most important ‘non-litigation strategy’ for competition agencies, helping competition agencies ‘spur business rivalry.’<sup>6</sup> Its importance has been highlighted by practitioners from around the world;<sup>7</sup> it is recognised as a designated, distinct form of competition policy implementation within many competition agencies;<sup>8</sup> and in 2013, the World Bank established an annual Competition Policy Advocacy Contest to recognise exceptional advocacy work by competition agencies.<sup>9</sup>

Advocacy is now recognised as an important and distinct part of competition policy because it promises to foster market competition in ways traditional competition law enforcement cannot. For instance, by educating policymakers, consumers, and business (wo)men about the benefits of the market process, advocacy seeks to foster the somewhat amorphous but important “culture of competition.”<sup>10</sup>

Competition advocacy, moreover, “unmask[s] the social costs” of laws and regulations that intentionally or inadvertently restrict market entry (domestically or transnationally), restrict price competition, create monopolies or dominant positions in a market or create bottlenecks in

value chains – and presses public officials to justify restrictions that have such anticompetitive effects. In doing so, advocacy targets what may be the most important impediments to market competition: in developing countries governmental distortions of the market in the form of exclusive privileges and selective interventions, through which a privileged few gain at everyone else’s expense.<sup>11</sup>

Accordingly, the ICN and others consider advocacy one of the most important objectives of competition advocacy to inhibit, or at least reduce, “rent-seeking.” As defined by Krueger in her seminal article, rent-seeking constitutes exploiting – or seeking the creation of – government restrictions in order to transfer wealth to the rent-seeking agent.<sup>12</sup>

As highlighted subsequently by Bhagwati, lobbying or otherwise inducing legislators or regulators to implement rules that make it harder for existing competitors to sell their goods or for new competitors to enter the market may be perfectly legal political behavior, but such rent-seeking or “directly unproductive profit-seeking” is distortionary and wasteful, since it uses time and resources to transfer rather than create wealth, i.e. without producing any additional goods or services.<sup>13</sup>

### **The Relationship between Competition Law, Advocacy, and Rent-Seeking**

Ironically, effective competition law enforcement may increase the need for policies that inhibit rent-seeking. As Tullock suggested in “The Welfare Costs of Tariffs, Monopolies and Theft,”<sup>14</sup> individual economic actors and firms may be thought of as allocating resources and efforts between productive activities and alternative ways of achieving gains, such as lobbying for protective tariffs or competition-inhibiting regulations. Applying a standard political economy framework, Tullock argued that the choice should be a function of the perceived relative payoff of the available strategies. If the expected utility of lobbying for government intervention (i.e., the rents that are obtainable from government intervention, multiplied by the probability of obtaining the intervention through lobbying) is large, relative to the expected utility of productive activity, we should expect rent-seeking. Tullock, therefore, posits that “domestic producers [will] invest resources in lobbying for the [rent-producing measure] until the marginal return on the last dollar so spent [is] equal to its likely return producing the transfer.”<sup>15</sup>

Rodriguez and Menon apply this logic to the realm of antitrust law and policy in their chapters on “The Political Economy of Antitrust Enforcement” and “The Limits of Competition Advocacy.”<sup>16</sup> Building on earlier work by Rodriguez with Coate and Williams,<sup>17</sup> they develop a model of the trade-off between rent-seeking and organising private cartels,

which yields the expectation that effective competition law enforcement encourages firms to resort to rent-seeking to make up for the loss of profits otherwise (or previously) obtained through anticompetitive actions:

The establishment of an antitrust regime may cause an increase in other forms of government protection. ... If the activities of an antitrust agency only make it more difficult to cartelise privately, the special interest group [that consequently] is ‘worse off’ than before [will] at the margin, ... seek more rents through government protection. [... Ultimately,] interest groups will choose that combination of private collusion and [lobbying for] government protection which maximises expected benefits.<sup>18</sup>

Note, however, that the baseline against which Tullock’s model works — investing resources and efforts into productive activity — has dropped out of Rodriguez and Menon’s model. If we restore that option, we get a choice set (for each producer) that consists of (i) investing in productive activity, (ii) investing in lobbying for rent-producing government intervention (we will call this “government protection” from market competition), and (iii) investing in anticompetitive behaviour, such as price-fixing, market-sharing, or bid-rigging (which we will call “private protection”). If we now apply standard political-economic reasoning to this choice set, we see that lowering the probability of achieving a given level of government protection-induced rents through lobbying — while also lowering the probability of achieving gains through private protection due to competition law and enforcement (as assumed by Rodriguez and Menon) — should reduce the amount of resources invested in seeking government protection as well as the amount invested in private protection *and instead increase investments in productive activity*.

The implication of this line of reasoning is that, for competition policy to yield the desired economic benefits, competition law enforcement needs to be combined with policies that reduce the incentives to invest in lobbying for government protection, i.e. to engage in rent-seeking. So how might competition advocacy lower the rents that can be achieved through (lobbying for) competition-reducing government intervention in markets — or lower the likelihood of achieving those rents?

Competition advocacy is, above all, concerned with monitoring the impact of state action on competition and minimising any unnecessary negative impact.<sup>19</sup> To do so, competition authorities may review existing and proposed laws and regulations, advise regulatory bodies or executive agencies on how to achieve the most pro-competitive implementation of law and policies, and generally raise awareness of the benefits of market

competition among policymakers, business executives, and the general public (and awareness of the conditions that are conducive to achieving those benefits). In doing so, competition agencies seek to convince the legislature and the executive ‘to abstain from adopting unnecessarily anticompetitive measures, and to help regulatory agencies clearly delineate the boundaries of economic regulation.’<sup>20</sup>

They may do so directly — e.g., by alerting legislators and government officials to the (possibly unintended or unrecognised) anticompetitive and hence rents-producing effects of existing or proposed policies, laws, or regulations — as well as indirectly, by making the economic costs of anti-competitive measures publicly known. Competition advocacy thus should not only reduce the willingness of public interest-oriented legislators and government officials to be responsive to the demand for government protection from rent-seeking interest groups, but, *ceteris paribus*, it should also increase the political costs of affirmatively responding to rent-seeking demands, which should reduce the responsiveness even of entirely self-interested public officials and thus reduce the likelihood that lobbying would be successful. In principle, then, competition advocacy is a promising and indeed necessary complement to competition law enforcement.

There is, however, one problem with relying upon competition agencies to provide a counterweight to interest groups that might lobby legislators or government (executive branch) officials for protection: Competition agencies are, as Rodriguez and Menon point out, themselves part of the government. And the members of the legislature, as well as the elected officials in the executive branch who would be the prime targets for rent-seeking lobbying arguably also to have at least some leverage over the competition agency.<sup>21</sup>

Sometimes this susceptibility to influence attempts by political leaders is a matter of bureaucratic hierarchies, such as when an agency is subordinate to a government ministry, or when the agency leadership serves at the discretion of the head of government. In other cases, susceptibility exists as a matter of democratic accountability, such as when agency representatives are required to appear (and answer questions) before committees of the legislature. And almost always, government leaders have some influence via the budgeting process and at least initially via the personnel appointment process. Advocacy powers therefore may need to be explicitly defined and mandated in the law in order for competition advocacy to have a chance of providing an effective counterweight to rent-seeking lobbying for anti-competitive legislation or regulations.

### **From Theory to Hypotheses**

This brief discussion of our theoretical approach allows us to specify two hypotheses with observable implications. First, by providing information to political leaders about the benefits of maintaining competitive markets and the harm of adopting anti-competitive laws and regulations, competition advocacy reduces the political attractiveness of the anti-competitive (rent-seeking) measures demanded by special interests. A veto-right for the competition agency may even outright prevent the adoption of such measures. This leads to:

H<sub>1</sub>: The more a competition authority engages in competition advocacy—and the stronger its advocacy role – the less effective will be any attempts of lobbying government officials or legislators for exclusive benefits (rents).

In keeping with the assumption of the theoretical model developed above, according to which firms engage in rent-seeking only for instrumental reasons, i.e. only when investing resources in rent-seeking promises greater gains than investing those resources into productive activity (or possibly other forms of anti-competitive behaviour), we expect the reduction in the effectiveness of rent-seeking to also reduce the incentives to engaging in rent-seeking in the first place:

H<sub>2</sub>: The more a competition authority engages in competition advocacy – and the stronger its advocacy role – the less firms should engage in rent-seeking.<sup>22</sup>

### **Empirical Analysis**

Assessing the relationship between competition advocacy and rent-seeking empirically requires us to overcome several challenges. First, there is no readily available, well-established measure of rent-seeking lobbying by firms — our outcome of interest. Second, neither scholars nor the international networks of antitrust agencies have created a measure of competition advocacy powers and practices for a broad range of countries.<sup>23</sup>

We overcome these challenges (with some caveats) and present what is, to the best of our knowledge, the first systematic empirical analysis of competition advocacy as an anti-rent-seeking policy in a developing or transition economy. For a measure of rent seeking, we take advantage of

the World Bank’s “Productivity and Investment Climate Private Enterprise Survey,” which between 2002 and 2005 (only) in some countries contained up to three questions that pertained specifically to firms’ lobbying activities.<sup>24</sup> Specifically, two questions (45a and 45b) asked respondents (i.e., business owners and senior managers) about the effectiveness of attempts by firms in the respondent’s industry to “gain advantages in the drafting of laws, decrees, regulations, and other binding government decisions” by lobbying members of the legislature or the executive, respectively. The two questions and the response options offered for each of them were:

In many countries, firms are said to give unofficial, private payments or other benefits to public officials to gain advantages in the drafting of laws, decrees, regulations, and other binding government decisions. To what extent have the following practices had a direct impact on your business?

- (a) Private payments or other benefits to Parliamentarians to affect their votes.
- (b) Private payments or other benefits to Government officials to affect the content of government decrees.

RESPONSE OPTIONS FOR EACH QUESTION: NO IMPACT [0];  
 MINOR IMPACT [1];  
 MODERATE IMPACT [2];  
 MAJOR IMPACT [3];  
 DECISIVE IMPACT [4];  
 NOT APPLICABLE;  
 DON’T KNOW

In addition, one question (44a) asked directly about the respondent firm’s lobbying activities to “influence the content of laws or regulations.” The exact question wording was (emphasis in the original):

Think about national laws and regulations enacted in the **last two years** that have a substantial impact on your business: Did your firm seek to lobby government or otherwise influence the content of laws or regulations affecting it?

RESPONSE OPTIONS: YES OR NO

None of these three questions by itself fully captures rent-seeking behaviour, but they provide – subject to the usual caveats regarding elite



surveys – quite good measures of several aspects of rent-seeking, which should be both valid and reliable across countries and over time.<sup>25</sup> In Ukraine, the three questions were asked, as part of a battery of questions about business-government relations, in both 2002 and 2005, allowing for a (quite short) over-time analysis.<sup>26</sup>

### **The 2003 Reform of the Ukrainian Competition Regime and Its Effect on Rent-Seeking**

Ukraine gained independence from the Soviet Union in August 1991. Ukraine enacted its first competition law in 1992, as part of sweeping political and economic reforms that entailed the transition of the previously state-dominated economy to a capitalist market economy, including privatisation of many previously state-owned enterprises. AMC Law, followed in 1993, establishing Ukraine's Anti-Monopoly Commission (AMC).<sup>27</sup> While the virtual absence of a state apparatus at the moment of independence<sup>28</sup> in some respects left the country with what the 2013 UNCTAD peer review described as “some of the highest barriers to the formation of an effective competition policy system”<sup>29</sup> it also made it possible to establish a new bureaucracy unencumbered by prior commitments – to the point that the AMC by the early 2000s became one of the most respected, professional parts of the Ukrainian public administration.<sup>30</sup> An independent regulatory body (whose chairman, however, was until recently appointed and dismissed by the President of Ukraine at his/her discretion), the AMC was given both prosecutorial and adjudicatory authority, including the power to conduct investigations, prosecute offenses of the competition law, and issue decisions.

The privatisation process was successful insofar as, by 2005, the private sector accounted for 85 per cent of industrial output and 74 per cent of employment.<sup>31</sup> The liberalisation efforts were substantially undermined, however, by a lack of transparency in public administration, so much so that Boner and Kovacic's 1997 analysis reports a widespread perception that government leaders, contrary to their “strong outward commitment to pursue radical, market-oriented reforms,” were in fact manipulating or extensively intervening in markets to generate private benefits (that is, rents) for various special interests through actions such as regulatory discrimination.<sup>32</sup>

Writing in 2000, Sundakov confirms this assessment, noting that the obscurity and vagueness of Ukrainian business laws and regulations leads to excessive administrative discretion and ‘creates an incentive for entrepreneurs to divert resources [away from productive activities] to attempts to bypass legal requirements.’<sup>33</sup> These problems were

compounded by high concentrations of economic power in many industries, as well as pervasive corruption at the individual level, which was getting increasingly institutionalised: “Each [oligarchic business] group has representatives in the Parliament and in the political parties to support its interests, and often also control mass media sources.”<sup>34</sup> In short, Ukraine in the early 2000s was a country much in need of effective competition advocacy. But could the AMC supply such advocacy?

From the time of its establishment, the AMC has from the time of its establishment had authority to engage in advocacy activities at all levels of government. Under Article 7 of the 1993 Law, the Commission had the power to make recommendations to Parliament and any executive agency for the amendment of laws and regulations that impede competition, the implementation of measures to limit monopoly, and the termination of measures that may have an adverse effect on competition. Moreover, Boner and Kovacic point out that the AMC’s structure has always been particularly conducive to competition advocacy in that the Chairman of the Commission is a member of the Cabinet of Ministers.

“In this forum,” Boner and Kovacic write in 1997, “the AMC has been extraordinarily active, if not always successful, in attempting to influence new legislation and structural reform in Ukraine ... [and] has taken a number of steps to counteract the tendencies of state bodies to impede competition and private sector development.”<sup>35</sup> Under the original 1993 law, however, the targets of such recommendations were only obliged to consider the proposal; they were free to reject it, as long as a rationale for the rejection was provided.

By the early 2000s, the AMC often therefore and increasingly found itself out-manoeuvred by rent-seekers and corrupt officials. This resulted in an amendment to the AMC Law in 2003, which significantly increased the AMC’s authority in the realm of competition advocacy.<sup>36</sup> The new provision, Article 20.4, was designed to bolster the AMC’s capacity to ensure that state agencies act in accordance with Article 15 of the Law of Ukraine on the Protection of Economic Competition, which prohibits any action that confers an unfair advantage to one business entity over another.<sup>37</sup>

Under Article 20.4, “the bodies of state power, bodies of local self-government, bodies of administrative and economic government and control” are required to obtain AMC approval for any “draft regulatory legal acts and other decisions that could lead to the limitation or distortion of competition, in particular.” This requirement is broad in scope, applying to any government action “that may result in prevention, elimination, restriction, or distortion of the competition in relevant markets.”<sup>38</sup>

Crucially, Article 20.4 renders the AMC's opinions on decisions that may impact competition *binding*, forbidding recipient agencies from implementing regulations or decisions in the absence of AMC approval.

The 2003 reform thus significantly strengthened the formal-legal authority of the AMC in the realm of competition advocacy. And the AMC appears to have made use of its increased authority promptly, rejecting about seven per cent and imposing conditions on another 14 per cent of the draft regulations, laws, and resolutions reviewed between 2003 and 2005.<sup>39</sup>

For example, when the local government in Ternopil in 2003 set fees for outdoor advertising, which were twice as high for advertisers from outside Ternopil than for locals, the AMC stepped in, forcing the local government to abandon the discriminatory fee structure. Similarly, when two government ministries developed a new health regulation requiring the disinfection of rail cars after the transport of foodstuffs, which included a short list of specific firms that allowed to provide these disinfection services (despite the availability of a substantially larger number of companies offering such services), the AMC intervened to replace the list with a provision that allowed anyone to provide the required disinfection services, as long as they meet the relevant, general technical standard.<sup>40</sup>

Given that the reform strengthening the AMC's advocacy powers was launched after the first World Bank enterprise survey in Ukraine was conducted in 2002 and fully implemented by the time the second survey was conducted in 2005, data from the two surveys allows us to analyse the effect of a significant strengthening of competition advocacy within the same country over a relatively short period of time.<sup>41</sup>

### Statistical Analysis

Given the operationalised dependent variables and the changes in the Ukrainian competition law between 2002 and 2005, we seek to assess the following operationalised hypotheses by comparing the responses to questions 45a, 45b, and 44a from the World Bank survey from the 2005 survey in Ukraine to the responses from the 2002 survey in Ukraine:

H<sub>1</sub>: Given that the 2003 reforms granted the AMC something akin to veto power over laws and regulations that might have an anti-competitive effect – thus explicitly defining and mandating stronger advocacy powers for the AMC – we expect a reduction in the perceived effectiveness of lobbying both legislators and government (executive branch) officials from 2002-2005.

H<sub>2</sub>: Given that the 2003 reforms strengthened the AMC's advocacy role, we expect to find a smaller share of firms in 2005 having recently attempted to influence the content of laws or decrees to their benefit than in 2002.

Table 3.1 reports the results of difference of means tests for questions 45a and 45b, as well as two-sample test of proportions for question 44. We find that the perceived effectiveness of rent-seeking lobbying declined between 2002 and 2005 — to a statistically clearly significant extent despite an already low baseline — both with regard to lobbying legislators and with regard to lobbying officials in the executive branch. Turning to the other survey question (44), we find that the share of Ukrainian enterprises whose representatives report having lobbied public officials to influence the content of laws or regulations affecting them, dropped from 26.8 per cent in 2002 to 16.3 per cent in 2005 — a substantively large and highly statistically significant decline in the level of rent-seeking.<sup>42</sup>

<b>Table 3.1: Differences in (Perceived Effectiveness of) Rent-Seeking, Ukraine (2005 vs. 2002)</b>			
	Perceived Effectiveness (0-4) of Lobbying...		Rent-Seeking: % Having Attempted
	Legislators	Gov. Officials	
mean <sub>Ukraine 2005</sub>	0.173 (537 obs)	0.202 (539 obs)	16.3% (594 obs)
mean <sub>Ukraine 2002</sub>	0.294 (401 obs)	0.332 (401 obs)	26.8% (462 obs)
difference [95% confidence interval]	-0.121** [-0.0242 -0.218]	-0.129** [-0.0300 -0.229]	-10.5%*** [-5.49% -15.5%]
z- or t-statistic	2.45	2.55	4.16
Note: The two "Perceived Effectiveness" columns show the average impact rating in 2005 versus 2002 for engaging in each of the noted forms of rent-seeking lobbying on a scale from 0 to 4, where 0 indicates "no impact" and 4 indicates "decisive impact." The "Attempted Rent-Seeking" column shows for each of the two surveys the percentage of respondents who answered the question affirmatively ("Yes"). The reported statistical significance is based on conducting the tests reported in the text: *** $p < 0.01$ ; ** $p < 0.05$ ; * $p < 0.1$ , two-tailed tests.			

Overall, the statistical analysis of the responses from the World Bank enterprise surveys in Ukraine suggest, with great consistency across the three different questions, that rent-seeking by Ukrainian firms became significantly less prevalent after the reform that strengthened the Ukrainian AMC. These findings yield strong support for both  $H_1$  and  $H_2$  — supporting the ICN’s assessment that ‘the possibility [of competition advocacy-conducting agencies] to influence the outcome of a policy or regulatory process is enormous whenever decision-making organs are obliged by law to heed the advice of the competition authority.’<sup>43</sup>

### **Developments in the Ukrainian Political Economy as an Alternative Explanation?**

Can we really attribute the reduction in reported and perceived rent-seeking between 2002 and 2005 to the strengthening of the AMC’s competition advocacy powers rather than broader developments in Ukrainian political economy? Ukraine experienced momentous political change between 2002 and 2005, but we submit that careful consideration of the most pertinent events and their precise chronology suggest that neither a specific event nor broader developments during those years provide a compelling alternative explanation.<sup>44</sup>

The 2002 enterprise survey was conducted between June 19 and July 31, 2002;<sup>45</sup> the 2005 survey between March 10 and April 20, 2005.<sup>46</sup> At the time of the 2002 survey, respondents would thus have known the outcome of the March 2002 Parliamentary election (though they were, strictly speaking, supposed to answer all questions based on fiscal/business year 2001, only); similarly at the time of the 2005 survey, they would have known political events through mid-April 2005 (but not later developments, and they were supposed to answer the questions based on developments through the end of fiscal year 2004, only). This suggests the following political context as potentially important:

The 2002 survey took place during the entrenched regime of President Leonid Kuchma (in office since 1994) and his prime minister, Viktor Yanukovych, built on Soviet-era political-bureaucratic and economic-administrative elite that was seen as largely captured by oligarchic clans and highly corrupt.<sup>47</sup>

After a political scandal that implicated Kuchma directly and personally in the abduction and murder of a popular journalist best known for publicising corruption in the government ended Kuchma’s ambition to run for a third term, the Presidential election of 2004 came down to a run-off vote on 21 November 2004 between Yanukovych and Viktor

Yushchenko. When, after reports of widespread voter intimidation, electoral fraud, and other irregularities during the run-off, the Election Commission declared Yanukovych the winner by three per cent, even though independent election monitors' exit polls had shown Yushchenko ahead by 11 per cent,<sup>48</sup> large and soon daily protests broke out in Kyiv and other towns across Ukraine. These protests became known as the "Orange Revolution," eventually prompting the Ukrainian Supreme Court to annul the November run-off and schedule a new vote for December 26, 2004, which Yushchenko won 52 per cent to 44 per cent. Yushchenko was inaugurated on January 23, 2005.

None of the events prior to Viktor Yushchenko's election or inauguration suggest any reasons to expect the substantial reduction in rent-seeking behaviour and effectiveness observed in the World Bank survey. The macroeconomic situation also changed very little between 2002 and 2005,<sup>49</sup> providing no reason to expect a reduction in rent seeking due to an increase in alternative profitable opportunities (see theoretical discussion above). The availability of an alternative explanation therefore hinges on the possibility that Ukrainian business survey respondents substantially revised their (reported) behavior and assessment of the efficacy of rent-seeking lobbying in response to Yushchenko's coming to power in the 3 months between President Yushchenko's inauguration on 23 January 2005 and the close of the WB survey on 20 April 2005. Although we cannot rule this out with certainty, it seems highly implausible, not just because of the mismatch between the shortage of time and size of the effect. As reported on Wikipedia, Yushchenko "was a charismatic candidate who [during the election campaign] showed no signs of being corrupt,"<sup>50</sup> and many—at least in the West—initially had very high hopes for the new regime.

But there were also, already at the time, accounts of the Orange Revolution that described it as a "revolt of the millionaires against the billionaires"<sup>51</sup> and merely a "reshuffle among the oligarchs,"<sup>52</sup> suggesting, if anything, an intensification of rent-seeking as a more numerous group of "new" insiders sought to become beneficiaries of the state's largesse. Later analyses also support this assessment when they conclude that the Orange Revolution did not in any substantial way change "the rent-seeking and rent-giving symbiotic relationship between President, Parliament, government, and big business"<sup>53</sup> and that "the new government also [soon] became tainted with corruption."<sup>54</sup> Transparency International's Corruption Perceptions Index for Ukraine also exhibits hardly any improvement between 2002 and 2005.<sup>55</sup>

In sum, the change in the assessed efficacy of rent-seeking lobbying, as well as in the frequency of such lobbying, summarised in Figure 1, appears to be indeed attributable to the boost in the AMC's competition advocacy powers.

That said, we want to emphasise that competition agencies – even well-resourced, relatively independent agencies, such as the Ukrainian AMC – cannot single-handedly defeat rent-seeking or deter corruption against powerful political forces, as developments in more recent years sadly illustrate: In December 2010, Viktor Yanukovich, the former prime minister on whose behalf the Kuchma regime had rigged the 2004 election triggered the Orange Revolution, succeeded in being elected President (with oversight powers over the AMC). He swiftly established what the OECD has called a “kleptocratic regime”<sup>56</sup> with rampant corruption at all levels of the state bureaucracy. Corruption reportedly also was found at the highest levels of the Anti-Monopoly Commission, eventually leaving the AMC demoralised and with a decimated budget and workforce – developments from which the agency is still trying to recover. Thus, although we see no reason to believe that the political context provides an alternative explanation for the observed change in the survey responses between 2002 and 2005, political context clearly matters.

## Conclusion

Seeking to influence public policy in accordance with one's interests is every citizen's right in a democracy. Those with highly concentrated interests, however, are often able to exercise highly disproportionate influence over the legislative and executive branches of government, resulting in laws or public policies that benefit the concentrated interests at everyone else's expense. And a pure market solution in the form of pushback from widely dispersed private actors is unlikely. As Rodriguez and Menon put it starkly: “No individual consumer in any nation affected by the proliferation of rent-seekers has an incentive (or wherewithal) to take action and to challenge those benefitting from government largesse.”<sup>57</sup> Authorising competition agencies to engage in competition advocacy is intended to re-balance the scales and make rent-seeking through anti-competitive laws, regulations, or decisions less likely.

This paper has presented the first systematic empirical analysis using non-US data to assess competition advocacy as an anti-rent-seeking policy. The findings suggest that competition advocacy indeed reduces the effectiveness of rent-seeking, and even the propensity to engage in rent-

seeking lobbying. On balance, this research thus suggests that competition advocacy holds much promise to increase both aggregate benefit from, and the number of beneficiaries of, a market economy. Governments seeking sustainable development should make such advocacy a priority, since rent-seeking is an important, common and often severe impediment to sustainable growth and development.

More broadly, our analysis suggests that non-enforcement strategies of implementing laws and regulation, such as competition law and policy in this case – can be highly effective. Yet, power or authority to engage in such non-enforcement actions may nonetheless need to be proscribed or backed up in law for such strategies to reach their full potential.



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## Endnotes

- 1 See Büthe and Minhas 2015 for a review.
- 2 Sanchez Ugarte *et al.* 2002: i, 25.
- 3 Sanchez Ugarte *et al.* 2002: 108. See also Rodriguez and Coate 1997: 368.
- 4 The problems with which the Ukrainian AMC has been struggling in recent years have been mostly just hinted at in English-language publications (see, e.g., Anonymous 2014; Denisenko and Lysenko 2015; Kenner 2015) but are well known among antitrust practitioners (not-for-attribution interviews, Washington, June 2015 and Geneva, July 2015).
- 5 For a brief account of support and opposition at that time, see Rodriguez and Coates 1997: 369f, n3-4.
- 6 Kovacic 2006: 541.
- 7 See, e.g., Sanchez Ugarte *et al.* 2002 and Hong 2014.
- 8 Dutz and Vagliasindi 2000: esp.766f.
- 9 World Bank Group 2014.
- 10 E.g., Fels and Ng 2013: 183. A culture of competition may be said to exist when there is a broad-based consensus in the private sector and more generally among the public, economic actors and state institutions that competition between economic actors is generally beneficial and normatively desirable as fundamental principle for the operation of the country's economy. See, e.g., Wilks 2007.
- 11 Kovacic 2006: 542, n6. See also Fox and Healey 2014; Jenny 2012.
- 12 Krueger 1974.
- 13 Bhagwati 1982.
- 14 Tullock 1967.
- 15 Tullock 1967: 228. Tullock thus implicitly recognises that there is a point at which investing resources in rent-seeking should cease, as the expected rents must be greater than the required inputs for lobbying to be perceived as profitable
- 16 Rodriguez and Menon 2010: 135-142, 159-166
- 17 Rodriguez and Coate 1997: esp. 372ff; Rodriguez and Williams 1994
- 18 Rodriguez and Menon 2010: 138, 164
- 19 See the ICN definition in the introduction to this paper.
- 20 Sanchez Ugarte *et al.* 2002: 31.
- 21 Rodriguez and Menon 2010: esp. 165f. See also Faith, Leavens and Tollison 1982; Wood and Anderson 1993.
- 22 Note that, in a perfect information equilibrium, the hypothesised reduction in attempted rent-seeking (H2) might overwhelm any observable reduction in effectiveness (H1). That is, the more limited rent-seeking that still takes place with a competition advocacy in place might exhibit no reduced rate of success compared to a baseline of having no (or only a weak) competition advocacy regime.
- 23 We thank senior officials of UNCTAD and long-term participants in the ICN for confirming this observation.

- 24 See World Bank 2002.
- 25 The two questions 45a and 45b might appear to blur the distinction between rent-seeking lobbying and corruption, but note that the World Bank survey asked clearly separately about corruption in questions 39 (about “gifts or payments” required to “get things done”) and 45d, which asks about *illegal* payments and benefits.
- 26 For reasons not known to us, the World Bank discontinued these questions after 2005.
- 27 The 1992 law is on file with the authors. The 1993 “Law on the Antimonopoly Committee of Ukraine” (with amendments) and the 2002 “Law on the Protection of Economic Competition” (with amendments) are contained, inter alia, in the *Compendium of Legislation of Ukraine on Protection of Economic Competition*, edited by the Anticompetitive Committee of Ukraine. Kyiv, 2012 (online at <http://www.amc.gov.ua/amku/doccatalog/document;sessionid=C1C7AB1FABB574BD5805320F15BCEACC?id=94745&schema=main>), 26-76 and 77-134, respectively.
- 28 Wilson 2005: 37.
- 29 UNCTAD 2013: 7.
- 30 OECD 2008: 76
- 31 OECD 2008: 9.
- 32 Boner and Kovacic 1997: 6, 25.
- 33 Sundakov 2000.
- 34 Makovskaya, Pridemore, and Nakajima 2003: 206. See also Matuszak 2012.
- 35 Boner and Kovacic 1997: 30; OECD 2008.
- 36 For a history of the revisions of the AMC Law, see WIPO 2016
- 37 2001 Law on Protection of Economic Competition.
- 38 Article 1, revised Law of Ukraine on the Antimonopoly Committee of Ukraine.
- 39 OECD 2008: 71 f
- 40 OECD 2008: 34
- 41 We will address possibly confounding developments in Ukrainian politics and economics between 2002 and 2005 below.
- 42 In interpreting the numbers in Table 1, such as the mean of 0.173 for lobbying legislators in 2005, keep in mind that, given the encoding of the variable, a mean of 0 for perceived effectiveness would indicate universal agreement that such lobbying has no impact, whereas a mean of 1 would indicate that, on average, such lobbying is seen as having “minor impact.”
- 43 Sanchez Ugarte *et al* 2002: 65.
- 44 This section draws, in addition to the specific sources noted, on a review of the various issues of the Economist Intelligence Unit’s *Country Reports: Ukraine* and the EIU’s *Country Profile: Ukraine* from 2001 through 2005
- 45 See MEMRB 2002: 3.
- 46 See Synovate 2005: 6.
- 47 Freyburg *et al* 2015:168f; see also Matuszak 2012.

- 48 Copsey 2004: 6.
- 49 OECD 2008: 9 f
- 50 [https://en.wikipedia.org/wiki/Orange\\_Revolution](https://en.wikipedia.org/wiki/Orange_Revolution) (last accessed 14 March 2016).
- 51 Aslund 2004: 9.
- 52 Matuszak 2012: 5.
- 53 Dimitrova and Dragneva 2013: 664.
- 54 D'Anieri 2010.
- 55 Ukraine's CPI point estimate and ranges (on a 0-10 scale, where scores between 2 and 3 indicate widespread corruption) were: for 2002: 2.4 (1.7-3.8); 2003: 2.3 (1.6-3.8); 2004: 2.2 (2.0-2.4); 2005: 2.6 (2.4-2.8); see annual Ukraine reports at [www.transparency.org/research/cpi](http://www.transparency.org/research/cpi) (last accessed 14 March 2016). See also the OECD's Anti-Corruption Network for Transition Economies' reports at <http://www.oecd.org/corruption/acn/istanbulactionplancountryreports.htm>
- 56 OECD 2015:5; others called it far worse, see, e.g., Riabchuk 2012.
- 57 Rodriguez and Menon 2010: 163.

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Part II:

# Country Experiences





# 4

## The Impact of Choice and Competition Reforms on Secondary Schools in Nigeria

AFOLAYAN GBENGA EMMANUEL  
*School of Education,  
Murdoch University, Australia*

### **Abstract**

Reforms to improve standards and reduce social segregation in schools have been in place in Nigeria for more than two decades. Some of these reforms reflect an increasingly market-inspired and competitive orientation. The paper intends to set out the impact of the specific reforms designed to increase parental choice and school competition in light of the government's continuing commitment to basic education.

To establish the context for these reforms, the paper will set out the objectives for, and economic arguments in support of, state-funded compulsory education, and highlights the government failures which prompted the introduction of an education quasi-market. Drawing on economic theory and evidence from Nigeria and internationally, the paper will focus on the central, and at times conflicting, issues of efficiency and equity, in particular in secondary schools.

Overall, the paper will argue that while the introduction of choice and competition reforms may have delivered some improvements to academic standards, this has likely been achieved at the expense of increased social segregation within schools. In particular, the paper will show that where the supply of good schools continues to be limited, schools have both the opportunity and incentive to 'cream-skim' the most able and privileged students.

In response to the growing trend of giving free rein to parental choice in the Nigerian education system, the paper will articulate the rationale for continuing government intervention in the education sector and, in conclusion, make recommendations on how best to develop this regulatory reform in ways which better promote social inclusiveness. Data would be drawn from the empirical literature and other relevant government and international publications.

## **Secondary Education: Objectives and Provision**

Secondary education provides a broad-based education for 12-17 years olds in Nigeria. The whole course falls into two parts – the first of three years' duration, marked on its completion by the Junior Secondary School Certificate Examination (JSSCE), the second of three years, with the Senior School Certificate Examination (SSCE). The secondary schools are run by a mixture of state and non-state providers, reaching millions of children – although there are still issues of access to education.<sup>1</sup>

Owing to the deteriorating state of education in the country, and the vision of the Federal Government to increase the access to quality basic education, the 'Universal Basic Education' (UBE) reform was launched in 1999. This represents the country's strategy and viable opportunity for achieving 'Education for All' (EFA). In particular, UBE reform provides for every Nigerian child, without exception, basic literacy and numeracy as well as knowledge of the culture of the society and the ability to communicate.<sup>2</sup>

In economic terms, education delivers both private and social returns, and the wider economic and social benefits in particular are at the heart of the objectives for public-funded schooling. In short, investment in the nation's people, or human capital, is deemed to lead to both increased economic productivity and improved social cohesion. Thus, the overarching objectives of public-funded schooling are to ensure that education is delivered as efficiently as possible to get the maximum economic and social benefit, and to do so in a way which is equitable.<sup>3</sup>

In one form or another, these objectives have been apparent in the Nigerian education system since the introduction of regional provision of education in the 1950s.<sup>4</sup> However, they have evolved over time to reflect changed economic and social circumstances, notably as part of the structural adjustment programmes (SAPs) and more recently in response to globalisation and economic crises. Since the return of democratic government in 1999, more emphasis has been laid on equity and efficiency, with a specific focus on effective delivery of education in light of increased

global competitive pressures.<sup>5</sup> The next section will critically examine the economic argument in favour of continued public intervention in secondary education.

## **Economic Case in Favour of Continued Public Funding For Secondary Education**

The effective and equitable delivery of educational benefits is also central to the economic arguments for education being predominantly funded by the state. In economic theory, government intervention is warranted in part when markets are considered to be inefficient in delivering a service, known as market failures, and in the case of education ‘externalities’ are the most common market failures used to justify state subsidy.<sup>6</sup>

Externalities, or spillovers, occur when individual or business activities affect others, who neither pay nor receive compensation for these benefits or costs.<sup>7</sup> In a market system, both consumers and producers are considered to be focussed primarily on their own ends, and this lack of concern for the wider effects of their actions is therefore considered to be a market failure.<sup>8</sup> In education, individuals may not always consider the wider costs and benefits of their education to society,<sup>9</sup> with the positive externalities defined by McMahon (2004: 211) as ‘the social or public benefits from the education of each individual that benefit others in the society in both current and future generations’.

On the other hand, there is consensus on the wider economic benefits which go beyond the improved productivity of individuals to encompass the positive impact that better educated employees can have on other workers and their organisations.<sup>10</sup> The wider non-economic social returns to education, however, are more contested. While Hanushek (2002:162, in Machin and Stevens, 2004) argues that details of social externalities are ‘noticeably elusive’, McMahon (2004) and Oreopoulos and Salvanes (2011) find considerable evidence of non-financial benefits such as improved health effects, reduced poverty and inequality and contribution to democratisation and political stability.

Imperfect information is another market failure used to justify public intervention. According to economic theory, for markets to operate efficiently they must provide consumers with adequate information to pursue their best interests; in the case of education government intervention is motivated in part “by the belief that consumers will not

possess complete information and that the market, by itself, will supply too little information.”<sup>11</sup>

For instance, if education were privately funded, parents would need enough information about both the costs and benefits of schooling to justify their investment and it is argued that since they may not be fully aware of the longer term benefits for their children, they are likely to give more weight to costs than benefits and underinvest in their children’s education.<sup>12</sup>

Likewise, institutions lending money to parents for their children’s education would find it difficult to assess which students were more likely to succeed in education, and therefore be able to repay loans, and would tend to favour the children of wealthier parents with assets to secure the loans.<sup>13</sup> These factors would tend to discourage significant take-up of education outside of the wealthy classes. Consequently, the problem of understanding the benefits of education, and the danger of underinvestment in education, provides justification for education to be made compulsory and subsidised.<sup>14</sup> In this way, education is thus referred to as a ‘merit good’, which ‘government compels individuals to consume.’<sup>15</sup> A case for public intervention in education is clear because the consumers might not make informed decisions for their future social welfare.<sup>16</sup>

Next, the need to promote equity rather than efficiency is another globally acknowledged justification for public intervention in education. As noted above, if parents were to pay for their children’s education, then the children of richer families, or those who valued education more highly, would be favoured and better educated. Children excluded from education would therefore be denied the individual benefits of schooling and the broader economic and social benefits of an educated population would be reduced.

Stiglitz (2000:427) notes that the “widespread belief that children’s access to education should not depend on their parents’ financial ability” provides the strongest argument in favour of public financing. This argument is essentially one of redistributing the educational benefit, and is grounded in Tobin’s (1970:264) concept of “specific egalitarianism”, in which access to certain goods “should be distributed less unequally than the ability to pay for them”. Le Grand (2007: 13) concurs and extends the equity argument to include social class, gender and ethnicity, reflecting that if on those grounds “some parents have preferential access to education for their children, then this is widely regarded as unfair or inequitable”.

## **Brief History of Education Reform in Nigeria**

Since 1955, educational reform in Nigeria has become an issue of focus for successive administrations, with the intention of providing universal, compulsory and subsidised schooling, although differences in emphasis have always existed in different regions and states. By 1976, the federal government became conscious of the global competitive advantages that proper education confers on citizens and therefore introduced the Universal Primary Education (UPE) scheme to replace the regional education reforms. Thus, the differences that had existed in the different regions (states) earlier were checked by the federal government.<sup>17</sup>

By the early 1980s, however, the UPE reform was widely seen as failing on both the efficiency and equity grounds, with concerns about regional social disparities, falling standard of the education and decline of educational infrastructures.<sup>18</sup> The predicament was also linked in part to funding, especially with the introduction of the SAP which necessitated reduction in social expenditure by government.<sup>19</sup>

These pitfalls that characterised the UPE reform led to the launch of the 'Universal Basic Education' (UBE) in 1999 to replace UPE. The reform seeks to universalise access of all children to educational opportunities for nine years.<sup>20</sup> Nevertheless, there are concerns about parental preferences for schools due to quality delivery and quality outcomes of UBE, poor infrastructures, irregular payment of teachers, inadequate funding and the widespread poverty, all of which factors are working against education.<sup>21</sup>

## **Educational Reforms: Objectives, Impact and Recommendations for Choice and Competition Policies**

For almost three decades, and most significantly since the 1976 UPE reform introduced genuinely 'UPE', the arguments above provided the foundation for compulsory schooling in Nigeria. By the mid-1980s, however, the public education system was widely seen as failing on both the efficiency and equity fronts, with concerns about low academic attainment and persistent social segregation in secondary schools. This problem of confidence in education was linked in large part to SAP-induced economic meltdown,<sup>22</sup> with widespread fear that Nigeria did not have an education system that could sustain economic competitiveness regionally and internationally.

By 1999, UBE reform was introduced. Although UBE was eventually passed into law in 2004, there were mounting concerns about the quality

of basic education in Nigeria.<sup>23</sup> For instance, there have been issues about the standard of UBE in terms of insufficient instructional facilities/technologies, inadequate teaching personnel, problem of curriculum implementation, among others.<sup>24</sup> Because of these problems Nigerian public schools are no longer option for the middle-class and rich parents who are able to enroll their children in private schools.

In 2004, UBE reform was officially put in place across the 36 states of Nigeria by the Act of Parliament (UBE Act) in order to address these failures in the public (basic) education system. It is believed that without sustainable reform, Millennium Development Goals (MDGs) and EFA desired goals cannot be achieved. UBE included a wide range of reforms covering components of national unified curriculum, parental obligations, funding responsibility (among three arms of government), and relegation of catchment areas together with more autonomy for schools.

Basically, the main objective of the choice and competition reform is to raise the quality of education through the introduction of market forces in terms of what is referred to as 'quasi-market.'<sup>25</sup> The quasi-market encompasses the market components of providers competing for customers; however, it is unlike the normal markets because such services are still paid for by the government, after user's choices have been ascertained. As noted by Le Grand (2007), quasi-markets circumvent the differential issues stemming from services that are only available to the people that can pay for them.

In education sector, choice and competition reforms mostly include parental capability to make a choice regarding the schools they prefer for their kids, together with sufficient funding for them. Schools are given greater managerial autonomy but still required to follow a national curriculum. In economic terms, such reforms are expected to improve educational outcomes for the same resource through increasing demand-side pressure from parents for good schools and giving supply-side flexibility to schools, in an attempt to allocate their budgets in such a way that would result in better educational attainments.<sup>26</sup>

However, one criticism that can be levelled at this outcome is that it is only the relatively well off and well-educated who want it and will be motivated to use it. Consequently, this reform might not have a positive impact on the equitable distribution of educational gains. There are evidential supports for this contention; however, studies in this area are very scarce in Nigeria, and one may have to rely on the literatures from the developed countries.<sup>27</sup>

International evidence has shown that there are mixed results for the impact of market reforms. As Hirsh (2002: 6) points out, 'policies

associated with school choice have nowhere proven to be a *magic bullet* to improve educational system but nor have they created a general catastrophe for education. Rather their effects have been specific and local'. What emerges from Hirsh's finding is that the impact of market reforms hinges on the way the education reforms are designed, introduced and localised in a particular context. Drawing on the experience from Nigeria, and internationally, the next section will examine in more detail the evidence in relation to the main objective of increasing educational efficiency through quasi-market reforms and any possible consequences this has for equity and social inclusiveness.

## Efficiency and Equity: Evidence from Nigeria and International Arena

Firstly, the international evidence on the impact of choice mechanism on educational efficiency is mixed. Some findings have shown increased efficiency while some cases with huge spending on education showed little or no improvement in academic achievement. For instance, Hirsh (2002) and Waslander et al (2010) find little evidence that market approaches are more effective in improving teaching and learning than other educational reforms.

In Nigeria, there is a consensus that exam results have partially or not improved in the past 10 years; yet the extent to which this can be ascribed to choice policies is challenging. There are challenging conclusions regarding the exam results of the students. Igbuzor (2006) and Asikhia (2010) note that academic performance (WASSCE results) have not improved because of the unqualified teaching force, gender issues and socio-cultural beliefs, and adherence to traditional assessment strategies. It then looks trickier to generalise the improvement of students' performance through exam results due to inconsistent evidence and wide disparities in Nigeria. Relevant in this regard, Gorard et al. (2003: 89) note that 'the evidence can do little more than suggest that this is an impact of market forces for there are so many other confounding changes over the same time'.

In the context of the quasi-market where schools compete for students, Burgess et.al. (2006:15) argue that schools "have the incentive to improve measured performance". However, that does not necessarily mean improvement in actual performance because there may be a tactical manipulation of behaviour to secure strategic advantage.<sup>28</sup> Selecting highly

performing students – known as ‘cream skimming’ – can result in better exam results, without actually improving effectiveness.

Globally, there is no evidence to show that choice policies reduce segregation. However, there are mixed findings in the levels of increases in segregation detected (Waslander et al, 2010; Le Gran et al, 2008). In Nigeria, schools that are most successful in terms of published market information have skewed student populations. As these assessments are modified by assumptions around the intersection of class, ethnicity, socio-cultural beliefs and gender, choice appears to lead to segregation and homogenisation of student populations.

For example, as some schools secure desired students and strong position in the marketplace, others become left behind with an under-supply of students, who are mostly from low socio-economic groups. These circumstances lock the latter category of schools in a series of poor academic achievement and student and teacher attrition, which has implication for choice policies. But in all these issues, Gorard et al (2003: 186) point out the possibility that ‘what choice policies may do is change the rules by which segregation takes place, but without markedly increasing or eliminating levels of segregation that are largely shaped by structural factors’.

Choice and competition policies, in an effective market, are expected to be mutually reinforcing. Here, the supply of schools increases or decreases in relation to demand. Nonetheless this, it appears not to work well in the quasi-market. Relevant to demand-side, parents do not react to underperforming schools by withdrawing their wards; and on the supply-side, popular schools do not easily meet the growing demand. Given the local problems (as mentioned earlier) in Nigeria, different reforms to increase social diversity in Nigeria have not generally and effectively corresponded with parental demand with school supply. This challenging process of choice by both parents and schools result in more segregated schools, pointing to the fact that when schools are over-subscribed, choice is efficiently usurped and annexed by schools, and none looks good for parents.<sup>29</sup>

Other elements for selection based on merit, state quota, exigency and environment intensify segregation. Segregation can also occur when such schools are mostly allowed to participate in the selection of the students; they tend to select relatively advantaged students and such a practice (cream-skimming) promotes inequality (see Gorard et al, 2003; Le Grand, 2007).

Educational reforms are not often about models, but outcomes. And since social processes are not always linear, it appears difficult to suggest



a definitive pattern of behaviour in educational reform strategies. Any model that attempts to explain the process of change, therefore, must rely on measure of outcomes of the process that reconciles equity, individualism, social mobility and equal opportunities. Therefore, if the choice policies are meticulously measured, it can help in exercising informed choice as to how to pursue, implement and improve these policies. International evidence shows that strategically measured choice policies with broader equity and social justice concerns have the potency to address segregation problem. In Nigeria, the control measures can embrace the geo-political and socio-economic mix in order to reduce social segregation.

## **Conclusion and Recommendations**

This paper has described the way education is delivered and funded. Taking account of the economic case for continued public intervention in the funding of education has also provided a new set of insights, positions and identities in consideration of which the roles of parents and schools are expected to change. The main objective of using choice and competition in the education system is to enhance academic achievement of students from both wealthier and low-income groups. Although neo-liberal ideas such as school choice reform policies can deliver outcomes in some circumstances, it does not apply to all situations and, as Hirsh (2002:21) has noted, it is ‘neither a cure-all nor a catastrophe for the quality of education’.

The impact of choice policies on school performance and student achievement is hotly contested. However, some of the evidence drawn from Nigeria reveals that exam results have not improved owing to such factors as social-economic and cultural forces and wilful motivations produced by published performance assessments. Though some international research offers some evidential support for beneficial effects, there is also a great deal of evidence showing no effects or negative consequences.<sup>30</sup>

That said, choice reforms appear to be ideal but the benefits have not been widespread because they carry with them dilemmas, including the way opportunistic and tactical behaviours have been apparent in schools, among parents and students. The evidence about education quasi-market also reveals that it has not boosted the chances of underprivileged children studying in better schools and also has not resolved the undue segregation between schools.

In Nigeria, access to secondary education continues to improve (courtesy of the introduction of UBE in 1999). At the same time, it

continues to be challenging, not only because of debates over the nature and role of secondary education but also because of differences in the ways stakeholders and policy-makers understand what constitutes access. Thus, inasmuch as the argument for continued public intervention in education is based on the equity concerns of educational benefits, the failure of market-driven policies to address segregation remains a challenging one, indeed. As challenging as the problem associated with choice policies can be, they can still help in reducing social segregation if those policies are appropriately implemented based on specific social contexts.

Based on what emerges from the findings in the paper, below are the recommendations that can fit in with the development of choice policies to achieve a reasonable measure of equitable outcomes in secondary schooling in Nigeria:

1. School supply: The educational stakeholders should devise effective assessment of the present policies aimed at cumulative supply of good schools in order to ensure the availability of appropriate incentives and structures for the expansion of good schools and establishment of new schools in the marketplace.
2. Performance measures: Concerned educational authorities should assess the performance measures to reduce the opportunities for schools to cream-skim students during admission period. The word limit for this paper has not given chance to thoroughly look at performance measures, though such measures together with choice reforms remain indispensable.
3. Regulation of Choice: Concerned authorities should adopt control mechanisms to address choice and equity concerns, particularly on the introduction of 'fair banding' as coined by West (2006) at grassroots' level to guarantee a better geo-political and socio-economic mix in schools. Taking away admission controls from schools also has the potential of circumventing any attempt at cream-skimming.

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## Endnotes

- 1 Ohia and Obasi, 2014; Ige, 2013; Olaniyan, 2011
- 2 Aluede, 2006
- 3 Le Grand et al, 2008; Stiglitz, 2000
- 4 Aluede, 2006; Adunola, 2011
- 5 Hinchliffe, 2002
- 6 Sun and Daniels, 2014; Le Grand et al, 2008; Stiglitz, 2000
- 7 Stiglitz, 2000
- 8 Le Grand et al, 2008
- 9 Temple, 2001
- 10 Cohen and Davidovitch, 2015; Le Grand et al, 2008; Machin and Stevens, 2004
- 11 Stiglitz, 2000: 83
- 12 Le Grand et al, 2008; McMahon, 2004
- 13 Le Grand, 2007
- 14 Grout and Stevens, 2003
- 15 Stiglitz, 2000: 87
- 16 See Machin and Stevens, 2004
- 17 Adunola, 2011; Amuda, 2011
- 18 Adunola, 2011
- 19 Moja, 2000
- 20 Oyinlola, 2012
- 21 Oyinlola, 2012; Amuda, 2011
- 22 See Odia and Omofonmwan, 2007
- 23 Fredriksen and Fossberg, 2014; Amuda, 2011
- 24 See Ige, 2013; Ogar and Aniefiok, 2012
- 25 Gorard et al, 2003
- 26 Burgess et al, 2006
- 27 e.g. Bradley and Taylor, 2002; Ball and Youdell, 2008
- 28 Ball and Youdell, 2008
- 29 Aluede et al, 2012
- 30 Supra Note 28

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## Making Competition Policy Work in Mexico

UMUT AYDIN  
Assistant Professor  
Instituto de Ciencia Política, Pontificia Universidad Católica de Chile  
Santiago, Chile

### Abstract

Mexico adopted its first competition law in 1992 in preparation for the signing of the North American Free Trade Agreement. Despite having provisions against monopolies in its constitutions of 1857 and 1917, a comprehensive law prohibiting cartels, preventing abuses of dominance, providing merger review, and an agency to implement these laws was a new phenomenon for Mexico. Moving quickly to 2015, the competition policy scene has dramatically changed in Mexico. The Federal Competition Commission (CFC) whose investigative powers significantly increased through reforms in 2006, 2011, 2013 and 2014 has become a well-respected enforcement agency that ranks above some Western European competition agencies with longer histories and much greater resources in Global Competition Review's (GCR's) annual rankings.

This paper explores the political factors that have contributed to the transformation of the Mexican competition regime from an ineffective regime in a highly concentrated economy into a relative success story. As an agency relatively well-endowed with financial and human resources in an upper middle-income country, the CFC has some advantages compared to agencies in poorer countries.

This paper investigates the sources of success of Mexico's competition regime with a perspective that emphasises both domestic and international

the politics of competition law reforms. Specifically, it explores how the CFC succeeded in gathering the political will needed to pass competition policy reforms that strengthened enforcement starting in 2006.

## **Introduction**

Mexico adopted its first competition law – the Federal Law on Economic Competition (FLEC) in 1992 in preparation for signing of the North American Free Trade Agreement (NAFTA). At the time few domestic actors knew what competition law meant and what impact it would have on them. For the Federal Commission of Economic Competition (FCC), the early years proved to be a period of trial and error. Actors within the government and the private sector criticised the Commission for being weak, court proceedings triggered by companies' complaints slowed down investigations, and a number of FCC's decisions were reversed by the district courts on procedural grounds.

By 2015, the competition policy scenario in Mexico had changed dramatically. The FCC's investigative powers significantly increased through a series of reforms starting in 2006, and it has become a well-respected enforcement agency that is held up as a model among the emerging economies.

This paper explores the political factors that have contributed to the transformation of the Mexican competition regime from an ineffective regime in a highly concentrated economy into a relative success story with a perspective that emphasises the politics, both domestic and international, of competition law reforms. Domestically, it is argued that a constituency in favour of better competition policy enforcement – composed of consumers, firms traditionally excluded from markets, and competition lawyers – gradually emerged and acquired voice in Mexico.

These favourable domestic conditions were reinforced by pressures generated by foreign firms seeking access to Mexican markets, and by the support of international organisations, such as the Organisation for Economic Cooperation and Development (OECD), the World Bank, the International Monetary Fund (IMF) and the International Competition Network (ICN). These organisations provided information, expert evaluations and political support for the FCC in its negotiations with domestic policy makers, and therefore, combined with domestic factors, enabled significant reforms of the Mexican competition regime.



## The Federal Law on Economic Competition

The proposal for a competition law surfaced in the context of the regulatory reforms of the late 1980s in Mexico. However, the idea of protecting competition in the market place dates back to the constitutions of 1857 and 1917. The Mexican constitution of 1857 prohibited monopolies, and the constitution of 1917, in addition, included provisions against cartels and abuses of dominance<sup>1</sup>. These provisions were not enforced due to the absence of implementing regulations, and in practice numerous state and private monopolies dominated the economy<sup>2</sup>. The 1934 Organic Law of Monopolies was likewise unenforced<sup>3</sup>.

Until the end of the 1980s, many businesses were shielded from external competition through the chambers of commerce, industry or by some level of government<sup>4</sup>. The degree of economic concentration in the economy was found to be high. In 1992, nearly 25 companies accounted for 47.1 percent of Mexican Gross Domestic Product or GDP<sup>5</sup>.

The debt crisis of 1982 motivated a number of institutional reforms through the rest of the 1980s and the 1990s. In the context of these reforms, officials at the Economic Deregulation Unit at the Secretary of Commerce and Industrial Development (SECOFI) became convinced of the necessity to adopt a competition law<sup>6</sup>.

Moreover, progress in the negotiations with the US and Canada on NAFTA provided an additional impetus for the adoption of a competition law, as NAFTA's Chapter 15 committed the parties to the adoption of measures proscribing anti-competitive business conduct. The process resulted in the adoption of the FLEC in the Mexican Congress in 1992 and the establishment of the Federal Competition Commission (FCC) as the agency responsible for its implementation in 1993.

The FLEC includes provisions against cartels and abuses of dominant position, and allows for merger review and competition advocacy. It classifies potentially anti-competitive practices as either absolute or relative. Absolute monopolistic practices include hard core cartels between competitors on price, output, market division and bid rigging, and are prohibited *per se*<sup>7</sup>.

What in other countries would be treated under monopoly or abuse of dominance provisions are treated as relative monopolistic practices, which might be found illegal only if the agents have substantial power in a defined relevant market<sup>8</sup>. Some of these are specified in the law, such as resale price maintenance, tied sales, exclusive dealing and refusals to deal, while others could be reached by the catch-all provision<sup>9</sup> that define 'any conduct that unduly damages, or impairs the competitive process and free access

to production, processing and distribution and marketing of goods and services' as anti-competitive<sup>10</sup>.

The FLEC prohibits mergers, which aim to reduce, distort or hinder competition<sup>11</sup>. All mergers that go beyond a certain threshold in terms of sales or assets have to be notified to the FCC<sup>12</sup>. In assessing mergers, the FLEC requires the FCC to consider whether the merging parties would be able to fix prices unilaterally, substantially restrict competitors' access to the market or engage in unlawful monopolistic conduct in assessing mergers.

State-owned enterprises are subject to FLEC's provisions on relative and absolute monopolistic practices, except in areas of 'strategic concern', which Article 28 of the Mexican constitution lists. Other than these exceptions, the FLEC applies to all economic actors, public or private. In fact, the FCC has brought cases against *Petróleos Mexicanos* (Pemex) despite the company being a state-owned monopoly in a strategic sector.

The FCC interpreted the constitutional provision as applying only to Pemex's role in oil exploration and refinement, and charged the company for abusing its dominance in the market for distribution by forcing companies that bought its gas to also use its transport network.

The FCC can give its opinions if another organ of the state acts in a way to restrict competition, but the opinion has no binding effect<sup>13</sup>. The FLEC empowers the FCC to give its opinion on the effects that existing legislation, regulations, and administrative acts might have on competition, and upon request by the Federal Executive, on the effects of competition on new laws and regulations proposed to the Congress<sup>14</sup>.

## Early Experiences

A number of obstacles to the effective implementation of the FLEC in the early years originated from the provisions of the law itself and the powers granted to the FCC under the law. First of all, the FCC had few tools to address problems in the highly concentrated sectors of the economy. The FLEC did not allow the FCC to restructure monopolies, which might have been a reasonable decision given the lessons drawn from the experience of other countries<sup>15</sup>. However, it soon became clear that a lack of powers to address structural monopolies could be problematic in a country like Mexico with a highly concentrated economic structure.

In addition, the division of responsibilities between sector regulators and the FCC proved problematic. The FCC was responsible in identifying whether a firm has market power in a sector, but it was up to the sector

regulator to address this behaviour after the decision of the FCC, with the FCC not being party to the negotiations or the preparation of regulation to deal with the anti-competitive conduct. This division of responsibilities became problematic if the sector regulator was too weak, or ‘captured’ by the actors whose behaviour it was supposed to regulate, or did not have any power to sanction the actors<sup>16</sup>.

The investigative powers granted to the FCC were also widely perceived to be inadequate<sup>17</sup>. The FCC did not have powers to conduct dawn raids, and it did not initially count on a leniency programme, which impeded its efforts to fight cartels. Moreover, the maximum fines it could impose (and effectively collect) were not deemed adequate to deter firms from engaging in anti-competitive conduct. Prior to the 2011 reforms, *The Economist* (2010) commented that it was profitable for firms to cheat even if caught.

In addition to the weaknesses of the legislation, the judicial system in Mexico had a significant impact on the effective implementation of the FLEC. Under the FLEC, the parties to a competition case had ample opportunities for judicial review if they were dissatisfied with the FCC’s decisions<sup>18</sup>.

The first of these is the *amparo* (injunction) action, which can be claimed by anyone arguing ‘that he is being subjected to an unconstitutional statute or that his due process rights are being infringed’<sup>19</sup>. *Amparo* claims were used aggressively and in increasing numbers by private actors against the FCC, and complicated competition law enforcement.

They delayed the FCC’s proceedings, as firms frequently filed multiple claims in different districts or filed subsequent *amparos* throughout the proceedings. For instance, after the FCC declared TELMEX to be a dominant carrier in 1998 – a necessary step for the sector regulator to step in and impose remedies – its decision was stayed by a series of *amparos*, changes to its declaration, and further *amparos*, until finally a court annulled the FCC’s decision in 2006 because the evidentiary basis for it was outdated<sup>20</sup>. *Amparos* might also delay the collection of fines, taking away the ‘bite’ of FCC’s decisions. Dealing with the *amparos* filed against it has imposed a significant strain on the agency’s resources.

A second way in which the parties to a FCC case could seek judicial relief was through an appeal to the Federal Court of Fiscal and Administrative Justice. This court normally reviews tax cases, but it asserts jurisdiction to review any agency action that involves the imposition of a monetary payment obligation on a private party, and it has thus reviewed a growing number of cases in which the FCC imposed fines<sup>21</sup>.

The FCC lost a number of cases under this court on the grounds that its orders imposing fines were not adequately justified. The OECD (2004, 47) reports that due to judicial and procedural intricacies of the system, the FCC was able to collect only 9.5 percent of all the fines it imposed between 1997-2002, with 18.5 percent revoked or lost on judicial review, and 72 percent remaining uncollected.

A few broader issues with respect to the judiciary have affected the implementation of the FLEC. The unfamiliarity of the district courts with substantive antitrust issues was one of them. In its early years, the FCC saw many of its decisions reversed at the district courts, mostly on procedural grounds<sup>22</sup>.

In addition to the judges' unfamiliarity with competition policy issues, the civil law model in Mexico "has traditionally involved detailed legislative enactments, and courts are unused to dealing with a statute as short and non-specific as the FLEC. By ruling adversely on a procedural point, the court can send the case back to the FCC and avoids resolving the antitrust question"<sup>23</sup>.

Critics also raise questions about the weakness of the judicial system in Mexico in resisting outside pressures, especially those coming from big business. In their empirical analysis of *amparo* requests in competition cases<sup>24</sup> find that companies directly or indirectly controlled by billionaires were more likely to secure an *amparo* from the courts compared to other firms. They cautiously interpret these results as supportive of their claim that concentrated business interests have undue influence in the Mexican judicial system.

This does not necessarily mean that the judicial system is corrupt, as big business also commands significant resources to hire the best law firms to defend itself. Del Villar (2009, 334) notes that the FCC's annual budget is equal to two days' worth of profits by TELMEX and RadioMóvil Dipsa (TELCEL), the two big companies that dominate the landline and cellular phone markets in Mexico, both controlled by Carlos Slim.

## **Reforms to the FLEC**

Reforms in 2006, 2011, 2013 and 2014 have addressed some of the problems that impeded the effectiveness of Mexican competition regime. The 2006 reform introduced a leniency programme. It also enabled the FCC to impose structural remedies, such as divestitures in monopoly cases, and expanded the list of relative monopolistic conditions listed in the Article 10 of the 1992 FLEC<sup>25</sup>. With the 2011 reforms, the FCC acquired

powers to conduct dawn raids. The FCC's fight against cartels was reinforced additionally by expanding the scope for criminal prosecution against individuals in cartel cases.

The 2011 reforms strengthened the FCC's deterrent power by increasing maximum fines from US\$7min to 10 percent of the firm's annual revenues in Mexico. The reform granted the FCC with more flexibility to reach settlements with parties while the investigation is ongoing, while before it could only come to a settlement after concluding its investigation<sup>26</sup>.

The FCC was also granted with the power to issue interim measures, by which it can oblige firms to cease alleged anti-competitive conduct while an investigation is carried out. Finally, class actions for damages in competition law cases were allowed<sup>27</sup>.

The competition regime in Mexico saw its most fundamental reforms in 2013 and 2014 in the context of the Pact for Mexico. After being elected to office in 2012, Enrique Peña Nieto announced the Pact for Mexico, an agreement between the three main parties on a broad package of reforms including in education, taxes, the economy and the legal system. Such a sweeping reform agenda became possible thanks to internal politics of the two opposition parties, and Peña Nieto's skillful management of powerful interest groups and private actors<sup>28</sup>.

In the oil and gas sector, the reforms included changes to the constitution that allow for private and foreign investment in refining, pipelines, petrochemicals, transportation and storage of oil, gas and petroleum products.

In telecommunications, the reforms created the Federal Institute of Telecommunications (IFETEL), an independent legal entity to regulate the telecommunications and broadcasting, and made this agency responsible for competition matters in these two sectors.

The IFETEL can impose one-sided regulations on firms that it finds to be dominant in these markets. The law also removes the 49 percent limit on foreign ownership of telephone services, and raises the limit of foreign ownership to 49 percent in broadcasting, which opens the way for greater foreign investment.

The competition policy reform started in 2013 with constitutional amendments that changed the legal status of the FCC, reconstituting it as a legally independent entity under the Mexican constitution. The reform established specialised courts to oversee appeals to competition law and telecommunications cases.

The *amparo* requests in these areas are also to be resolved by these specialised courts. In 2014, the Mexican congress adopted a new

competition law, as implementing regulation to the 2013 constitutional amendments. The new FLEC creates an investigation unit within the FCC in order to separate investigative authority from decision-making authority.

The law further strengthens the FCC's powers by expanding the scope of evidence that it can collect through dawn raids, and increasing the fines it can impose. The new law expands the list of relative monopolistic practices. Finally, an important change is that FCC resolutions are not subject to a judicial stay pending the outcome of litigation.

What explains the gradual strengthening of the Mexican competition law through legislative and constitutional reforms since 2006? My argument is that the interplay of a number of domestic and international factors has brought about the reforms. Domestically, consumers and firms that have been traditionally excluded from concentrated markets have generated pressures for better competition law enforcement.

Consumers' interests arise from the potential benefits competition might bring in the form of lower prices. Economic concentration hurts Mexican consumers, especially the poorest sectors of the society, which devote 7 percent of their spending to overcharging by firms with market power<sup>29</sup>. However, consumer interests are diffuse and hard to mobilise.

Historically, very few consumer organisations existed in Mexico, but the situation is gradually changing with the emergence of non-governmental organisations, such as the Observatel, the watchdog of regulatory reforms in the telecoms sector<sup>30</sup> or *Controlaría Ciudadana*, which monitors public policies, such as competition policy and the fight against corruption.

The FCC has also entered into an agreement with the Office of the Federal Prosecutor for the Consumer (PROFECO) in 2005, providing for more cooperation and coordination between the two organisations and more direct channels for the FCC to hear about consumer concerns. PROFECO has the right to introduce the equivalent of class action suits in competition cases, and has brought two such cases recently against dominant landline and cellular phone companies TELMEX and TELCEL to attempt to recover money on behalf of millions of consumers<sup>31</sup>.

Domestic firms that have difficulty entering markets dominated by large players create another source of pressure for better competition law enforcement. For instance, Avantel, a Mexican cellular provider sued TELMEX nine times for abuse of dominant position<sup>32</sup>.

Finally, domestically competition lawyers and bar associations have become important actors with a stake in the proper functioning of the system, for instance by helping to provide training to Mexican judges in competition matters.

International pressures for reforming the Mexican competition law have reinforced these domestic demands. Foreign firms have been a source of pressure for the Mexican government to improve the effectiveness of competition laws. For instance, in 2000, the US government brought a dispute against Mexico in the World Trade Organisation (WTO), principally on behalf of AT&T and MCI, claiming that its telecoms regulations breached its obligations under the General Agreement on Trade in Services.

The Federal Commission of Telecommunications (COFETEL) had granted TELMEX, the firm with the largest share of outgoing calls, the power to fix the 'termination rate' to be paid by all foreign carriers, such as AT&T and MCI – for calls terminating in Mexico<sup>33</sup>.

The World Trade Organisation (WTO) ruled against Mexico, forcing COFETEL to change the regulation, with significant downward impact on international settlement rates and hence the price of international calls<sup>34</sup>.

Mexico's greater economic openness, and its bilateral, regional and multilateral trade agreements mean that foreign firms will increasingly be sources of pressure for access to domestic markets and generate pressures for better enforcement of competition laws. In fact, the recent reforms allowing for greater foreign ownership in telecoms companies allowed AT&T to acquire the third and fourth large players in the mobile phone market in Mexico, generating pressures for better services and lower prices<sup>35</sup>.

A significant impetus for the broader reform agenda in Mexico has been the desire to increase the competitiveness of the Mexican economy. International organisations, such as the IMF (2006), the World Bank (2007) and the World Economic Forum have repeatedly emphasised lack of competition as a significant impediment to growth. The recommendations of these organisations are frequently reported in the national media and become part of the public debate, and have thus been important input for reforms.

Organisations, such as the OECD and the ICN have had an even more direct impact on the reform process in Mexico. The OECD Competition Commission has worked closely with the FCC. Through its peer reviews, the OECD provided a neutral voice to the discussion by presenting a non-partisan analysis of the state of competition policy in Mexico and simply outlining best practices based on its experience in the area with OECD member countries.

The OECD report was used and cited in communications with the legislature and federal public administration”. The OECD also provided lengthy comments on the draft of reforms. The ICN similarly was influential in ensuring that reforms to the Mexican competition law followed international best practices.

Despite many positive aspects of the recent reforms, there have also been some controversial areas where the most recent Mexican law departs from international practice. For instance, in order to better address monopolies, which most experts agree are an important problem for the Mexican economy and Mexican consumers, the FLEC prohibits ‘barriers to competition’, defined as any structural market characteristic or conduct that limits the access of competitors or interferes with free competition.

‘Barriers to competition’ as a concept has been criticised for being too vague and without foundation in mainstream competition law and economic theory<sup>36</sup>. Furthermore, the FCC is given the power to conduct market studies and impose behavioural or structural remedies if ‘barriers to competition’ are found to exist in a sector. This is criticised as being an ‘extreme intervention’ into the working of the markets<sup>37</sup> and potentially a responsibility that could overburden the competition agency and undermine its independence<sup>38</sup>. In 2014, the FCC undertook a ‘resource-intensive’ market study of the financial sector, for instance, which took energy away from enforcement efforts<sup>39</sup>.

The 2014 reforms gave the FCC the power to identify and regulate access to ‘essential inputs’, essentially setting maximum prices for infrastructure, which gives it a vague and sweeping authority<sup>40</sup> (Phillips 2014). This provision is also problematic because it might create disincentives for firms to invest in infrastructure<sup>41</sup>. Finally, the reforms give jurisdiction over competition in the telecommunications sector to the newly-established and constitutionally independent IFETEL, which might prove problematic.

Sector regulators tend to have regular and closer relations with the players in the sectors that they regulate, which might undermine their independence. In the European context, Petit (2004) has also raised questions about potential overlaps and jurisdictional confusion with the multiplication of sector regulators along competition authorities. It will be crucial to ensure a harmonious working relationship and cooperation between the IFETEL and the FCC in the coming years.

There have also been some practical issues in competition enforcement in the aftermath of the reforms. The FCC has seen some significant staff turnaround, with seven new commissioners taking charge in the first year of reforms, and eighty-four competition enforcers leaving the FCC in



2013, and fifty-six in 2014<sup>42</sup>. The agency has also had to devote substantial resources to institution building, which resulted in modest enforcement in 2014<sup>43</sup>.

Some observers have also complained that FCC investigations have slowed down during this time of adaptation. Nonetheless, the FCC boasts high success rate at the courts in the last two years and is contributing successfully to the Mexican legislative and administrative process through its competition advocacy.

It has also enjoyed a boost to its budget of 32 percent for 2013 and 60 percent for 2014<sup>44</sup>. These positive developments and its increased powers set the FCC on a solid path for good enforcement. Together with the National Development Plan 2013-2018, which emphasises the need for an industrial policy that seeks to “deepen and strengthen market competition as the main tool to build a dynamic economy”, competition policy in Mexico should contribute to the competitiveness of the Mexican economy<sup>45</sup>.

## Conclusion

After adopting a modern competition law in 1992, Mexico struggled to enforce this law effectively in its first decade. The FCC encountered many problems, such as legislative loopholes, insufficient powers to conduct investigations and to sanction breaches, insufficient financial resources, defeats at the district courts, and the frequent use of *amparos* that significantly delayed the conclusion of proceedings and strained the scarce resources of the agency.

The early problems of the Mexican competition regime draw our attention to the difficulty of making foreign legal transplants work in contexts where the local institutional setting, combined with powerful private and public interests can easily frustrate efforts. Mexico’s problems in enforcing its competition law are fairly typical among new competition regimes.

A series of reforms starting in 2006, and culminating in a fundamental revamp of the law and the FCC in 2014 have addressed many of these problems. What made the reforms possible in the Mexican context were pressures from an emerging domestic constituency for a more competitive economy reinforced by pressures and guidance from international organisations and foreign firms. This analysis of the reform process draws attention to the importance of encouraging competition policy to spread its roots in the domestic system and supporting those roots through international assistance and guidance.

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## Endnotes

1 Avalos 2006; Castañeda 1998

2 *Ibid*

3 *Ibid*

4 *Ibid*

5 Newberg 1993, 603

6 Avalos 2006, 10

7 OECD 1998, 10-11

8 en Kate and Niels 2006, 719; OECD 1998

9 Article 10 paragraph 7

10 OECD 1998, 12; Pérez Motta and Sada Correa 2013, 11

The explicit list of relative monopolistic practices has been extended in subsequent reforms of the FLEC. This was partly a reaction to a Supreme Court decision taken in 2006 that found the catch-all provision too vague to be a basis for an FCC decision.

11 OECD 2004, 25

12 Ogletrophe 2014

13 OECD 2004, 15

14 OECD 1998, 25

15 OECD 1998, 13

16 OECD 1998, 32

17 OECD 2004, 65

18 OECD 2004, 44

19 *Ibid*

20 Noll 2009, 382

21 OECD 2004, 46

22 OECD 2004, 45

23 *Ibid*

24 Guerrero, López-Calva and Walton (2009, 129)

25 OECD 2011b, 128

26 OECD 2011a, 4

27 OECD 2012, 4

28 Starr 2014, 32

29 Urzúa 2013

30 Malkin 2014

31 Garcia de la Rosa 2014, fn. 15

32 Guerrero, López-Calva, and Walton 2009, 129

- 33 Fox 2006, 276
- 34 del Villar 2009, 340
- 35 Reuters 2015
- 36 Perrot and Komninos 2014,
- 37 *Ibid*
- 38 Supra note 10
- 39 Global Competition Review 2015
- 40 Phillips 2014
- 41 Perrot and Komninos 2014, 11
- 42 Global Competition Review 2014, 2015
- 43 Global Competition Review 2015
- 44 Supra note 42
- 45 Moreno-Brid 2013, 218

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## 6

# Competition Law and Sustainable Development in China

WENDY NG

*Lecturer, Melbourne Law School,  
The University of Melbourne, Australia*

### Abstract

Since embarking on economic reform and opening up in 1978, China has achieved remarkable economic growth, with an average GDP growth rate of 10 percent during 1978-2006, and absolute poverty has decreased significantly as a result. However, this rapid and high economic growth has also resulted in a number of social and environmental problems.

Recognising a need to change its mode of development, since 2006 and especially since the adoption of the Twelfth Five-Year Plan (2011–2015), the Chinese government has focused on achieving sustainable development, encompassing economic, social, and environmental goals. One of the tools available to the Chinese government to help it promote and achieve sustainable development is its competition law, called the Anti-Monopoly Law, which came into effect in August 2008.

The paper will examine whether and how the Chinese government has promoted competition law, policy, and reforms and enforced the Anti-Monopoly Law, with a focus on how the Chinese government has used competition law and policy to address issues relating to sustainable development. The paper begins by looking at the ways and context in which competition law, policy, and reform are discussed within and by the Chinese government (especially the competition agencies) and how it is linked to other government policies, goals, and priorities. The paper then analyses the enforcement activities of the Chinese competition

authorities, in particular looking at the industries affected, types of competition policy instruments used, geographic scopes of concern, and nature of the competition restrictions targeted. Such analyses are conducted with a view to evaluating how the Chinese government has used competition law and policy to help promote sustainable development.

## Introduction

Since embarking on economic reforms and opening up in 1978, China has achieved remarkable economic growth, with an average gross domestic product (GDP) growth rate of 10 percent during 1978-2006,<sup>1</sup> and absolute poverty has decreased significantly as a result.<sup>2</sup> However, this rapid and high economic growth has also resulted in a number of social and environmental problems. For example, inequality in China has almost doubled since 1981 and its Gini coefficient has remained at a relatively high level of between 0.47 and 0.49 in the past decade, according to official figures.<sup>3</sup> Pollution and environmental degradation have led to public health and environmental issues, and in 2008 it was estimated that environmental degradation and resource depletion cost China approximately nine percent of its gross national income (GNI).<sup>4</sup>

Recognising a need to change its mode of development, since the adoption of scientific development and socialist harmonious society by the Chinese Communist Party (CCP) and especially since the implementation of the Twelfth Five-Year Plan (2011–2015), the Chinese government has focussed on achieving sustainable development rather than aggregate economic growth and the absolute living standard. China's sustainable development strategy encompasses economic, social, and environmental goals including enhancing scientific and technological development and innovation, improving people's wellbeing and livelihood, reducing poverty, improving the environment, resource use, and development ability, and coordinating the development of the economy, society, people, resources, and the environment.<sup>5</sup>

The Chinese government has often referred to its competition law as one of the laws that is essential to helping it to promote and achieve sustainable development. Called the *Anti-Monopoly Law*<sup>6</sup> (AML), it came into effect in August 2008 and, similar to the competition laws of adopted by many other countries, prohibits horizontal and vertical anticompetitive agreements,<sup>7</sup> abuses of dominance,<sup>8</sup> and anticompetitive mergers.<sup>9</sup> In addition, the AML prohibits anticompetitive abuses of administrative power<sup>10</sup> (also known as administrative monopolies), which are regarded as major barriers to furthering economic reforms.<sup>11</sup>

This paper examines the role that competition law and policy plays in achieving sustainable development outcomes in China. The paper first considers how competition law and policy is linked to the reform and development agenda in China. It then explores how the AML has been implemented by the Chinese competition agencies to help promote and achieve sustainable development outcomes.

## **Relationship between Competition Law and Policy and China's Reform and Development Agenda**

Competition law and policy has long been linked to China's broader government reform and development agenda. Since the socialist market economy was officially recognised in March 1993, competition and the market mechanism have been viewed as essential to China's socialist market economy and the promotion and furtherance of China's economic reforms and opening up.<sup>12</sup> Indeed, promoting the healthy development of the socialist market economy is one of the express objectives of the AML.<sup>13</sup>

Competition law is viewed as an essential part of a legal system that is required to support the functioning of a market economy.<sup>14</sup> The Chinese government believes that the AML provides a basic framework that helps to establish competitive market structures, promote and ensure competitive conduct, and guide the future direction of China's economic reforms.<sup>15</sup> It also helps to maintain fair and orderly market competition by eliminating market distortions, rectifying disorderly market competition, and providing clear, transparent, and predictable standards of conduct.<sup>16</sup>

Competition law and policy is also coordinated with other policies and priorities to jointly promote and achieve economic, development, and other outcomes.<sup>17</sup> This coordination role of competition law and policy is referred to in Article 4 of the AML.<sup>18</sup> In China, competition law serves broader macroeconomic goals and is viewed as a tool that can be used by the government to intervene and achieve particular outcomes.<sup>19</sup> Although the government recognises that the market plays the decisive role in allocating resources in the economy, it nonetheless remains subject to the macroeconomic control of the socialist state.<sup>20</sup>

Discussions of competition law and policy often occur in the context of specific development and reform goals and priorities. These include innovation and innovation-driven development, people's wellbeing and livelihood, and price regulation and stabilisation. These matters are explored in this section.



**Innovation and Innovation-driven Development**

The promotion of innovation has become an increasingly important aspect of Chinese competition law and policy. The Chinese government recognises that competition plays a fundamental role in encouraging innovation by providing incentives for businesses to innovate, which, in turn, promotes economic development and transformation.<sup>21</sup> Competition law is also regarded as part of the institutional environment that fosters innovation.<sup>22</sup>

This increased emphasis on innovation in competition discourse is consistent with the growing importance of innovation to China's reform and development strategy. The Chinese government has made it a priority to transform China's economic development model into one of sustainable development and China's economy into an innovation economy.<sup>23</sup> In 2006, it launched a major 15-year programme to develop science and technology and promote innovation.<sup>24</sup>

In November 2013, the CCP adopted a wide-ranging reform blueprint at the Third Plenum of the 18<sup>th</sup> Central Committee of the CCP and recognised that innovation is key to deepening science and technology structure reform.<sup>25</sup> Following on from the Third Plenum, the CCP and the State Council jointly adopted an innovation-driven development strategy in March 2015, which focusses on creating an institutional environment (of which the market is one) conducive to innovation.<sup>26</sup> Innovation will also be a focus in the Chinese government's Thirteenth Five-Year Plan, which will be finalised by the National People's Congress in March 2016 and apply from 2016 to 2020.<sup>27</sup>

The focus on innovation is part of the Chinese government's goal to shift its development model from one focussed on economic growth to one that is sustainable, and to move China from traditional, low technology, and low value-add activities into more innovative, knowledge-intensive, high technology, and high value-add activities.<sup>28</sup> In particular, the Chinese government is focussed on indigenous innovation and encourages Chinese businesses to develop their own technology and products.<sup>29</sup>

The Chinese government aims to decrease China's reliance on imported intellectual property (IP) and technology and narrow the technology gap between China and other countries.<sup>30</sup> However, it also believes that indigenous innovation is built upon a foundation provided by foreign IP and technology, and there are some concerns about the conduct of these foreign IP and technology holders.<sup>31</sup>

### People's Well-being and Livelihood

The Chinese government expressly relates competition law and policy to the improvement of people's wellbeing and livelihood. Officials at Chinese competition agencies have stated that their competition enforcement priorities are industries related to people's wellbeing and livelihood such as consumer goods, public utilities, telecommunications, pharmaceuticals and transportation.<sup>32</sup> They believe that anticompetitive conduct in these sectors, which all relate to essential goods and services, affects people's lives and harms China's economic development.<sup>33</sup>

The enforcement of competition law in essential goods and services such as staple foods, housing, public utilities, transportation, and other basic infrastructure services can help to ensure that people have access to goods and services that are lower priced and of higher quality. In particular, poorer people are more vulnerable to higher prices that result from a lack of competition in these industries, as they tend to spend a higher proportion of their income on essential goods and services than wealthier people.<sup>34</sup>

### Price Regulation and Stabilisation

The Chinese government regards competition law as part of the legal system that regulates prices, maintains price stability, and curbs inflation.<sup>35</sup> In turn, price regulation and competition enforcement serve the needs of macroeconomic regulation and control.<sup>36</sup>

As China's economy has shifted from being a planned to a socialist market economy where the market plays a decisive role in allocating resources, the government's role in the economy has also changed. The government determined the prices of all products under the previous planned economy. In contrast, under the current socialist market economy, less than five percent of the total retail sales of consumer goods are either guided or pre-determined by the government.<sup>37</sup>

However, this shift to market prices does not mean that the government has no pricing-related role in the market. Rather, the government has changed its function to one of supervision and regulation of pricing conduct *ex post*.<sup>38</sup> Competition law is a law that the government can apply to carry out this price supervision and regulation role.

The relationship between competition law and the pricing regulation system is reflected in the fact that the National Development Reform Commission (NDRC) is one of the three competition agencies in China.<sup>39</sup> The NDRC's AML enforcement role is price-specific, as it is responsible for enforcing the AML to address price-related non-merger conduct. In addition to being a competition agency, the NDRC is also responsible for

regulating the prices of certain key commodities and controlling and stabilising the general level of prices under the *Price Law*.<sup>40</sup>

The department within the NDRC that is responsible for the AML is also responsible for price supervision. The NDRC has made it clear that it believes that its AML's enforcement activities will strengthen price regulation and maintain the stability of overall price levels.<sup>41</sup> It will also, in carrying out such work, consider matters such as new economic development strategies and challenges, innovation, social equality, and the development of the socialist market economy.<sup>42</sup>

## Competition Enforcement and Promotion of Sustainable Development

In the six and a half years since the AML has been in operation, the Chinese competition agencies have taken enforcement action across a variety of industries and against both small domestic businesses and larger, multinational companies. As of December 31, 2015, more than 1300 mergers have been reviewed, and an overwhelming majority of those mergers were approved unconditionally (1276 mergers, 97.85 percent), two mergers prohibited (0.15 percent), and 26 mergers conditionally approved (1.99 percent). Nearly 100 investigations or decisions relating to anticompetitive agreements, abuse of dominance behavior, and abuses of administrative power have been made.<sup>43</sup>

There is broad recognition that the Chinese competition agencies have made great improvements in their enforcement capabilities and practice in the past six years, although some commentators have criticised the Chinese competition agencies for unfairly targeting foreign companies and not conducting their investigations and reviews with sufficient due process and transparency.<sup>44</sup>

An examination of the AML enforcement activity to date reveals some enforcement priorities and patterns that suggest that the Chinese competition agencies are enforcing the AML in a manner that not only addresses concerns about anticompetitive conduct but also helps promote and achieve the sustainable development related goals.

## Innovation and Innovation-driven Development

Several enforcement investigations and decisions demonstrate that the Chinese competition agencies are using the AML to address issues relating to intellectual property rights (IPRs). The AML applies to the anticompetitive abuse of IPRs to eliminate or restrict market

competition,<sup>45</sup> which might fall under the prohibition of anticompetitive agreements, abuses of dominance, or anticompetitive mergers.<sup>46</sup>

In the merger context, the Ministry of Commerce (MOFCOM, which is responsible for merger enforcement under the AML) has looked at issues relating to IPR licencing in its reviews of Google's acquisition of Motorola Mobility,<sup>47</sup> Microsoft's purchase of Nokia's Devices and Sales business,<sup>48</sup> and most recently, Nokia's acquisition of Alcatel-Lucent.<sup>49</sup>

These transactions occurred in communications and technology-related markets, where the main barrier to entry is access to IPRs. The merging parties in each transaction owned a number of key IPRs. In Google/Motorola Mobility and Microsoft/Nokia Devices and Sales, the IPRs in question related to smartphone manufacture and smartphone operating systems, whereas in Nokia/Alcatel-Lucent, the merging parties held communications technology standard essential patents (SEPs).

In each case, the MOFCOM was concerned about the ability of smartphone manufacturers and other downstream businesses to obtain IPR licences. As IPRs are essential for entry into the relevant markets, refusal to grant licenses for these IPRs could harm competition.

A related concern was whether licensees would be able to resist or counter increases in or high licencing fees. To address its concerns, in both the Google/Motorola Mobility and Microsoft/Nokia Devices and Sales transactions, as condition to its approval, the MOFCOM required the merging parties to, *inter alia*, provide access to certain categories of IPRs on a fair, reasonable, and non-discriminatory (FRAND) basis and maintain existing licencing practices for some other types of IPRs.

Additionally, the MOFCOM required that Microsoft not increase its licencing fees on specific non-SEPs for eight years. In the Nokia/Alcatel Lucent acquisition, the MOFCOM required that Nokia confirm that it would not seek injunctions to prevent the use of SEPs granted on a FRAND basis and to make certain commitments to its licencees and potential licencees in China when transferring a SEP to a third party.

Similarly, IPR licencing fees and practices were the subject of the NDRC's investigations of Qualcomm<sup>50</sup> and InterDigital.<sup>51</sup> Both companies hold SEPs for wireless communication standards. The NDRC was concerned that the companies had acted anticompetitively by, *inter alia*, charging unfairly high licencing fees, bundling the licencing of non-SEPs to SEPs, and requiring their Chinese licencees to cross licence their relevant patents free of charge. In both cases, the companies offered commitments to address these concerns. They each committed to not tie the licensing of SEPs with non-SEPs and to not require Chinese licencees cross licence their patents free of charge.

Qualcomm also stated that it would charge patent royalties based on 65 percent of the net wholesale price for smartphones sold in China (which represents a reduction in its royalty rate) and adopt a rectification plan to change some of its business practices in China and satisfy the NDRC's decision.<sup>52</sup> InterDigital also made a commitment to not charge discriminatory and high licensing fees to Chinese businesses.

In addition to undertaking investigations, the Chinese competition agencies have specifically considered IPR-related issues in their implementing regulations. In April 2015, the State Administration for Industry and Commerce (SAIC, which is responsible for non-price related non-merger conduct under the AML) issued regulations on the anticompetitive abuse of IPRs,<sup>53</sup> which took nearly six years to prepare. Just two months later, the Chinese government announced that an antitrust guideline on the anticompetitive abuse of IPRs would be prepared by the NDRC and adopted by the Anti-Monopoly Commission (AMC).<sup>54</sup>

The AMC is a cross-ministry body that sits under the State Council and was established to organise, coordinate and guide China's competition policy.<sup>55</sup> The fact that the AMC, rather than the Chinese competition agencies individually, will promulgate this guideline shows the importance attached to this issue by the Chinese government. Unlike the SAIC's IPR regulation, which is adopted only by the SAIC and not binding on the other Chinese competition agencies, once adopted by the AMC, the antitrust guideline will bind all three competition agencies. Further, the IPR antitrust guideline will be only the second regulation adopted by the AMC,<sup>56</sup> reflecting its significance.

The Chinese competition agencies' concern about IPR-related matters fits in with the Chinese government's emphasis on innovation and innovation-driven development. IPRs are essential to innovation and technological advancement, and the anticompetitive abuse of IPRs stifles innovation.<sup>57</sup> High IPR licencing fees are also thought to be not conducive to encouraging investment in research and development or the sustainable development of businesses.<sup>58</sup> Reflecting this view, in March 2015, the head of the Price Supervision and Anti-monopoly Bureau at the NDRC (the department within the NDRC responsible for AML matters) stated that abuse of IPRs will be the next major focus of its enforcement activities.<sup>59</sup>

Moreover, it is not surprising that the competition agencies' IPR-related enquiries have involved the telecommunications industry. Mobile communications is part of the new generation information technology industry, which was designated a new strategic industry that would be developed vigorously by the Chinese government in the Twelfth Five-

Year Plan (2011–2015).<sup>60</sup> China is also the world's largest producer and consumer of smartphones.<sup>61</sup>

The ability of Chinese smartphone manufacturers to obtain relevant IPR licenses, the level of IPR licencing fees (the cost of which may ultimately be borne by Chinese consumers), and licencing practices of IPR holders will influence China's ability to develop this strategic industry. These AML enforcement actions relating to IPR, however, have attracted some controversy, as there is speculation and concern that the AML is being used to reduce royalty payments and obtain better terms and conditions, bargaining power, and competitive advantage for Chinese licencees, and that the rights of IPR holders are being curtailed.<sup>62</sup>

### **People's Well-being and Livelihood**

The substantial majority of competition enforcement activity has occurred in sectors where people purchase goods and services, such as food and beverages, public utilities, information technology and telecommunications, health, automobiles and after-sales services, transportation, and other consumer goods. Such industries are important for people's wellbeing and livelihood as they relate to essential goods and services or people's day-to-day activities. This is consistent with the stated enforcement priorities of the Chinese competition agencies.

In particular, the SAIC and the NDRC have targeted cartels relating to materials used in the construction sector. The construction sector is vital to China's sustainable development. In China's first official urbanisation plan issued in 2014, the Chinese government stated that urbanisation will drive sustainable and healthy economic growth in China, and it aims to have 60 percent of its population living in urban areas by 2020 (as compared to 53.7 percent in 2014).<sup>63</sup>

As such, the Chinese government, together with the private sector, has invested, and is continuing to invest, heavily in urban infrastructure such as housing, transportation networks, and public utilities.<sup>64</sup> One of the guiding principles of China's urbanisation plan is the decisive role of the market in resource allocation.<sup>65</sup> The enforcement of the AML to remove anticompetitive conduct in the construction sector is consistent with China's urbanisation and sustainable development aims.

Further, the construction industry impacts people's wellbeing and livelihood. In addition to building public infrastructure and services that will be accessed by the public, the construction industry is a large employer, especially of migrant workers who are typically poor, from rural areas, and leave their hometowns to work in other places for a majority of the

year. In 2013, the total number of such migrant workers in China was 166.10 million,<sup>66</sup> and it was reported that one in five migrant workers worked in the construction industry.<sup>67</sup>

### Price Regulation and Stabilisation

A number of the NDRC's investigations and decisions reflect the view that the AML and the *Price Law* are part of a suite of laws that helps it regulate and supervise prices. The NDRC has relied on the AML and the *Price Law* simultaneously to investigate and sanction price-related conduct, especially in the early years of AML enforcement. Such investigations include a rice noodle cartel in Guangxi Province,<sup>68</sup> a paperboard cartel in Zhejiang Province,<sup>69</sup> pricing conduct in the tourism industry in Hainan Province and Yunnan Province,<sup>70</sup> minimum shipping fees in the courier industry in Xiamen,<sup>71</sup> and pre-delivery inspection fees in the automobile industry in Wuhan.<sup>72</sup>

Further, more recently the NDRC has enforced the AML to address its concerns about pricing, independent of the *Price Law*, in a manner that is consistent with serving the macroeconomic control of the state. In the past couple of years, it appears that the NDRC has started to use the AML as an alternative to using interventionist or non-legal measures to carry out its price supervision role. Generally, the NDRC tends to promote the use of direct government intervention to address problems.<sup>73</sup> This is not unusual, given its history as the price-setting and economic planning authority under the planned economy. Typical measures used include freezing prices, restricting exports, or directly asking companies not to increase their prices.<sup>74</sup> In 2011, for example, the NDRC took such measures to help it control the prices of instant noodles, cooking oil, pork, flour, soap, detergent, washing powder, and shampoo products.<sup>75</sup>

The NDRC's propensity for intervention might be changing, as it seems to be increasingly relying on the AML to address pricing issues. For example, since 2008, the price of imported infant formula has increased substantially (reportedly by more than 30 percent) and imported infant formula has been in short supply.<sup>76</sup> The NDRC had, for the first few years, used interventionist approaches to address these issues, however they were ineffective in preventing the price of foreign infant formula from rising.<sup>77</sup>

The NDRC subsequently initiated an AML investigation into infant formula producers in March 2013.<sup>78</sup> In contrast to its previous interventionist efforts, this investigation resulted in some of the investigated infant formula producers committing to reducing prices even before the NDRC's decision was handed down.<sup>79</sup> The NDRC claims that its AML

investigation resulted in the nine investigated infant formula producers lowering their prices by more than RMB 2.4 billion in total.<sup>80</sup> The NDRC took a similar approach in 2014 to address concerns about the high prices of imported and foreign branded cars and auto parts in China and investigated a number of foreign car manufacturers and their local dealers for potentially breaching the AML.<sup>81</sup> A range of car manufacturers very quickly reduced their prices in response to the AML investigation.<sup>82</sup>

## Conclusion

Whilst the Chinese government recognises that competition law and policy helps to promote and maintain competition and achieve better outcomes for consumers, competition law and policy sits firmly within the government's broader reform and development agenda. The Chinese government and the competition agencies expressly link competition law and policy with China's sustainable development goals, and much of competition law discourse in China is focused on the role of competition law in helping to improve people's wellbeing and livelihood, promote the pursuit of innovation by businesses, and regulate and supervise prices, with a view to macroeconomic regulation and control. This narrative of competition law and policy is corroborated by the enforcement actions taken by the competition agencies, as these sustainable development objectives are reflected in the investigations and outcomes that have been pursued by the competition agencies to date.

With this in mind, given the association between competition law and policy and the Chinese government's development and reform strategies, the future development and direction of competition law, policy, and enforcement in China may adapt and fluctuate with changes in China's development and reform priorities or as the structure of China's economy changes. The upcoming release of China's Thirteenth Five-Year Plan, for example, will not only provide detail about China's development priorities over the next five years but also shed light on the development of Chinese competition law, policy and practice in the near future.



## Endnotes

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Although it is beyond the scope of this paper to examine the merits of such complaints and concerns, it should be mentioned that the Chinese competition agencies, especially the MOFCOM, are working to address some of these concerns. For example, in response to complaints made by practitioners and businesses about the delays associated with merger review, in April 2014 the MOFCOM implemented an expedited review process for mergers that do not raise substantial competition concerns, which has substantially reduced the amount of time it takes for the MOFCOM to review and approve mergers in a majority of cases. The Chinese competition agencies have also taken steps to improve transparency by providing more information about their decisions and additional guidance on enforcement practices. For example, the NDRC is currently preparing six antitrust guidelines, covering issues such as intellectual property rights, leniency, and the calculation of fines. These guidelines, once finalised, will apply to all three competition agencies and should improve enforcement consistency across the agencies.

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# Contributions to Inclusive Economic Growth in Argentina

## *Integrating Design, Marketing and Entrepreneurship for Local Development in Buenos Aires Province*

FEDERICO DEL GIORGIO SOLFA AND MARÍA SOL SIERRA

*National University of La Plata;  
Scientific Research Commission of Buenos Aires Province &  
National University of Lomas de Zamora  
Argentina*

### **Abstract**

This work aims to study strategies used in Argentine local development experiences, focussing on industrial design, marketing and entrepreneurship. In order to this purpose, backgrounds are analysed with this approach adding the study of three strategic plans for national and provincial-level that are currently in force. With the analysis of the transport system in the last decade, an accelerated cost increase is evident, resulting in a relatively higher price of distributed products. This situation that was initially perceived as a disadvantage finally set up an opportunity to produce locally.

The goal of this paper is to provide tools that contribute to the work shipped by key institutions for local development (public, private and intermediary organisations), and the way these interact with the actors and the territory. In particular, the identification of productive sectors and the selection of goods that can be produced and consumed locally, as a key input for the formulation of projects.



## **Introduction**

The initiative inscribed as the zero step of the Improvement Scholarship project (Call 2014) of Technological Research Commission of the Province of Buenos Aires (CIC-PBA), has been evaluated successfully. The approach comprises the integration of design, marketing and entrepreneurship as an effective methodology for contribution to the local development in small villages.

Overall, the supplies considered are: 1. Strategic Industrial Plan 2020 (PEI)<sup>1</sup>; 2. Federal and Participative Agri-food and Agribusiness Strategic Plan 2010-2016 (PEA2)<sup>2</sup>; and 3. Strategic Productive Plan Buenos Aires 2020 (PEPBA)<sup>3</sup>. These strategic plans constitute the main political guidelines for national and provincial productive development.

The focus will be on strategies that allow to capitalise locally: territorial potentialities (endogenous) and exogenous favourable conditions, which comes from the national and sub-national context. Leading with this a local growth with development, this last one defined as territorial equity, social inclusion and environmental sustainability (Arocena, 2002).

## **Context and Industrial Policies**

In Argentina, after the conclusion of the last military process, happened between 1976 and 1983, a democratic cycle began. In it, successive institutional and political transformations called ‘first generation’ ones (related to human rights, new rights began and guarantees democracy under the rule of law) were experienced.

In the early 90s the called ‘second generation’ reforms were performed, driving the transformation of the state (affecting the operation of the market economy, opening the domestic market, privatisation, integration into the global world currency stability). It emerged with this a dynamic model that initially resulted in the deepening of the economic policy implemented by the military dictatorship (Azhiazu, 1994).

The change in external conditions, exhibited a strong vulnerability, generating more external and internal (social) debt, unprecedented levels of exclusion and growing social inequality.

In this context, a crisis occurred in 2001 that triggered the resignation of President Fernando de la Rúa, and presented a context of political and social instability. He was followed by transitional President Eduardo Duhalde, who transformed the government’s agenda, selecting problems and popular demands.

In this context, was implemented one of the first programmes aimed at developing the social economy and solidarity, the National Plan for Local Development and Social Economy *Manos a la Obra* (PMO)<sup>4</sup>: for the first time lines of work are set at national-level for recovering companies in the hands of their workers and aiming at strengthening local development (Srnc, 2009).

Thus began a tradition in socio-productive policies in Argentina, away from the welfare practice of the previous decade, foregrounding the local development and strengthening local power, the participation of citizens, nurturing ties between actors (*Ibíd.*). We identify actors as agents capable of producing changes in the territory. These can be individual or collective, of public, private or mixed type. Individual actors are workers, professionals, entrepreneurs, investors, etc.; while with collective actors refers to states, governments, businesses and Non-government Organisations (NGOs).

Cravacuore (2005) agrees with this, but stresses that at this phase the national government was decentralising the role of planner, giving way to local governments. In this process, these sub national governments were strengthened in this new role, although the actors continue awarding loans to the national-level.

The government of Duhalde was succeeded by the government of Néstor Kirchner and Cristina Fernández de Kirchner, prevalent until today. Pedrazzi (2010) argues that this government deepened measures established by Duhalde, progressing over this structure in the economic, political and social-level with a deepening of the model.

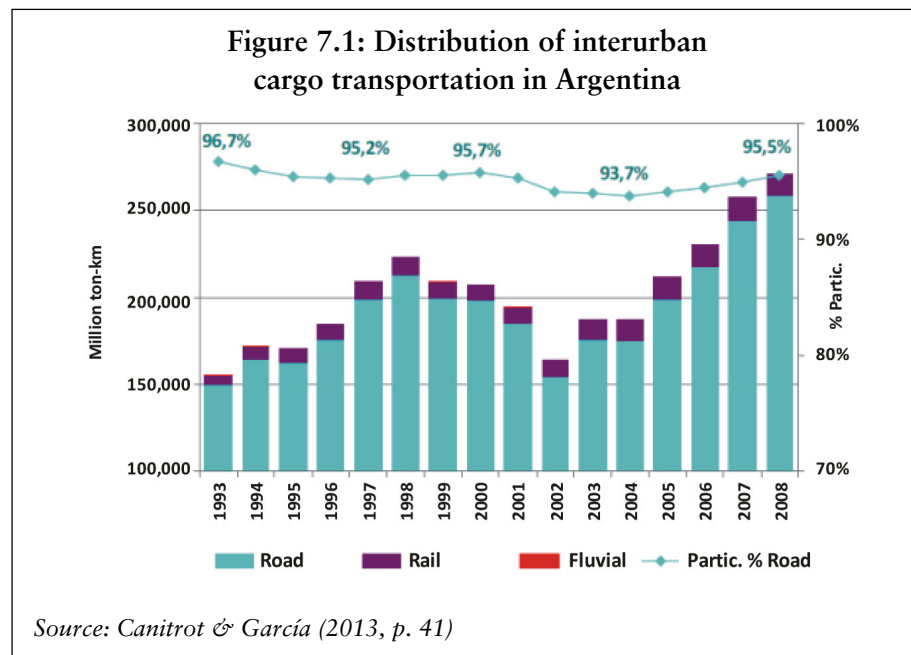
In this framework, was presented the PEA2, which promotes the participation of actors from different sectors in four Federal Councils, 23 spaces for interaction and dialogue between the provinces, 53 Faculties, national and international organisations and over 140 business chambers<sup>5</sup>.

In 2012, PEI was introduced with the aim of developing eleven industrial production centres in regional forums, with individual and collective actors, institutionally concatenating the nation, provinces, municipalities, public institutions and NGOs articulate collectively the Project (Ministerio de Industria, 2012).

## **Logistics and Transportation of Goods**

In the last decade, in a context of economic expansion, the transportation of goods found its highest level of costs (see Figure 7.1). On one hand, a railway system exclusively dedicated to transport commodities, and on the other, a goods transporting system that moves

95 percent of the country's cargo requirements, increasing (Canitrot & Garcia, 2013).



This situation led to an empowerment of workers and employees of the automotor transport loads sector, who obtained the highest increase in real wages over the last decade: 122 percent<sup>6</sup>.

These costs significantly influenced the final price of goods for use and consumption, thereby configuring a stage with greater opportunities for local development.

## Focussing on the Province of Buenos Aires

Taking as reference the PEI (national plan), in 2013 was agreed the PEPBA (provincial plan), which like national plans, promotes among its objectives: increasing productivity and exports, import substitution, reducing unemployment, industrialisation of the primary activities and boost to entrepreneurs and lagging regions by local development<sup>7</sup>.

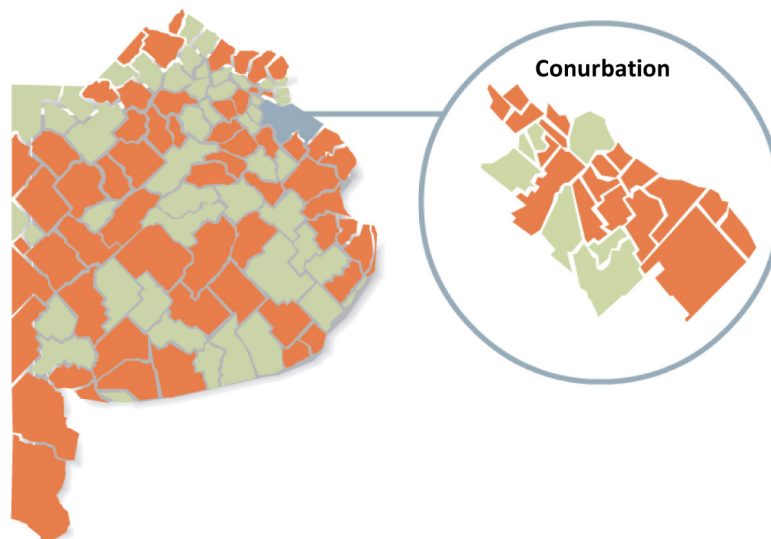
In the area of this province there are currently 87 Local Development Agencies, 15 Project Incubators and six Technological Poles.

Local Development Agencies are mixed public-private organisations that promote local production development and articulate the use of

instruments to support the competitiveness of enterprises, to energise the local production and economic activity (Kosacoff, 2008).

These organisations have the task of designing and implementing a specific territorial strategy, build an agenda of regional territorial issues and seek solutions in a framework of complementarity and public-private commitment. It is for these reasons, that Local Development Agencies can be conformed in all municipalities, according to the territorial scale required (see Figure 7.2).

**Figure 7.2: Geographical Distributions of Local Development Agencies of the Province of Buenos Aires**



Source: Ministerio de la Producción, Ciencia y Tecnología. [http://www.mp.gba.gov.ar/spmm/desarrollo\\_local/mapaprod/mapa\\_agencias.php](http://www.mp.gba.gov.ar/spmm/desarrollo_local/mapaprod/mapa_agencias.php)

Project Incubators are spaces of assistance to promote projects and ideas for sustainable productive enterprises. It is a tool to support the creation of new enterprises, which aims are to strengthen the productive fabric of the region.

Entrepreneur participants in these incubators, get linkages and strategic alliances for the promotion, development, consolidation and/or enhancement of their projects. Incubators also provide services, such as legal advice; physical space for conducting meetings or for the installation of the enterprise; participation in fairs and exhibitions; trade links; fundraising and mentoring business.

In addition, the Direction of Local Productive Development (provincial government), in conjunction with the Innovative Projects Incubator EMTEC, performs transfers methodologies.

From the different local scopes, industrial designers and marketing professional actors can be linked with the nearest incubators to their location, to get advice and support in the early stages of their enterprises. In this manner, incubators increase its outreach to a micro-regional scale.

**Table 7.1: Incubators of Buenos Aires Province**

Name of the Incubator	Municipality	State
EMTEC Innovative Projects Incubator	La Plata	Active
FRAY LUIS BELTRÁN Business Incubator	San Martín	Active
UNSAM Business Incubator	San Martín	Active
Olavarría Incubates	Olavarría	Active
Red Gesol	Hurlingham	Active
DINÁMINA SE	Tigre	Active
INCUEI	Luján	Active
Junín Business Incubator	Junín	Active
Olmos Undertakes	La Plata	In conformation
Coronel Suárez Business Incubator	Coronel Suárez	In conformation
INCUTEC	Berazategui	In conformation
Gender Incubator	La Plata	In project
Bahía Blanca Business Incubator	Bahía Blanca	In project
Azul Business Incubator	Azul	In project
Center for Development	De la Costa	In project
Source: Ministerio de la Producción, Ciencia y Tecnología. <a href="http://www.mp.gba.gov.ar/spmm/desarrollo_local/download/incubadoras_activas.xls">http://www.mp.gba.gov.ar/spmm/desarrollo_local/download/incubadoras_activas.xls</a>		

Technological Poles (PTs) located in the Province of Buenos Aires, are next to the National Universities, which have careers related to technology. These clusters act as articulators between human resources (scientists and technicians) of universities and the productive system, to develop solutions for the specific needs of each sector.

The PTs allows the development and technological innovation, combining the efforts of small and medium-sized enterprises (SMEs) to enhance their growth, creating jobs and promoting local and regional development<sup>8</sup>.

Thus, companies that are linked to a Pole, receive more benefits and possibilities to innovate, than other firms operating independently.

These PT, have the potential to configure productive development models and key business for each area of the Province of Buenos Aires. The holders of the different productive enterprises might eventually attend these centres of research and transfer home their projects, even if they are away from their local areas.

Table 7.2: Technological Poles of the Buenos Aires Province	
Ubication of the Technological Poles	State
1. Bahía Blanca	Active
2. Junín	Active
3. La Plata	Active
4. Mar del Plata	Active
5. Tandil	Active
6. San Nicolás	In project
<i>Source: Ministerio de la Producción, Ciencia y Tecnología.  <a href="http://www.mp.gba.gov.ar/spmm/desarrollo_local/download/polos_tecnologicos_activos.xls">http://www.mp.gba.gov.ar/spmm/desarrollo_local/download/polos_tecnologicos_activos.xls</a> </i>	

Local growth with development does not belong to any specific discipline, began as an interdisciplinary project of socio-economic research, and this is its main strength. Meanwhile, his weakness is that does not have a recognised theoretical framework, but rather its configured by the user, who can supplement it with his discipline (Sforzi, 2007).

In local development, the key is the involvement of civil society organisations in the taking of decisions, when plans for development of a territory are determined (Quetglas, 2008).

According to Cuervo (1999), who see the local field as an opportunity, agree to support their ideas-project in emerging advantages resulting from the valuation of own resources and synergies of growth and welfare, instead of waiting for extra local assistance.

The local development conceived as integrated, allows the system actors of a territory to jointly develop; also, constitutes a challenge to build a more just, prosperous and caring society<sup>9</sup>.

Our approach to local development -product of the study of several authors and empirical evidence-, argues that it must be expressed as

territorial equity, social inclusion and environmental sustainability, looking for a local growth with sustainable development (Thomas, 2012).

For Boisier (2001) the local development should be based on social capitalisation of resources and endogenous potentialities of a community or sector, in order to deal with exogenous variables that are unfavourable. Must be taken (social, technical, natural, cultural, institutional and economic) territorial capabilities in order to strengthen common projects, encourage the construction of a territorial identity and achieve social welfare, for the sustained growth of community solidarity.

Regarding emplacement of these policies, local development involves thinking the territory of a particular way: consider a small sector where minimum and indispensable actors manifest, belonging to the same identity portion, sharing a region and common values; achieved this, the territory where it will be project is conformed<sup>10</sup>.

For a territory interesting from a development perspective, Boisier (2001) defines that it should be organised, that is, having a community with administrative and political regulation, and local identity.

## **Actors, Institutions and Territory**

As mentioned before, local actors can be individual or collective. When we refer to collective actors, in the public scope we find: sub-national authorities (municipal, provincial and regional), universities, schools, training institutions, public financial institutions; and in the private sector: commercial chambers, associations, professional councils, financial institutions, workers' cooperatives, trade unions, private universities, NGOs, etc. These actors in order to be considered locals or territorials must indispensably share a defined spatial location.

To conform the territory where the local development will be projected, must be take a particular place or micro-region, looking at a bare minimum number of actors who share an identity and values (PEA2, PEI, PEPBA).

In this logic, to improve the interaction between the actors and territory different institutional plans are project and create. Strategic plans analysed, aimed at generating agreements among actors at different levels, to achieve a seamless and synergistic interaction.

The policies<sup>11</sup> share the same goal: that the primary links (producers who process the raw material, entrepreneurs and small businesses), achieve long-term profitability.

In our evaluation with this perspective, we find that as Madoery (2001, p.3) indicates, the social processes in contemporary society are produced

in dynamic, unique and unrepeatable space-time matrixes. Consequently, it's necessary to re-signify the role of actors – individual and collective, the features of social organisation and the context in which they operate; as the development decisional matrix can no longer be controlled only by state or market mechanisms.

Therefore, we consider that policies should be diagrammed where the involved society participate in the development process, framing it in the respective institutional and cultural environment.

These issues, are not yet precisely delineated on the most recent programmes. In this proposed scheme, we find on the subject of local development a mediating role.

## **The Subject of Local Development**

The subject of local development, is the figure of the protagonist and beneficiary of the development process. We say that he acts as a mediator because it has a role of territorial entrepreneur, which collects information from the environment and interact with other agents like entrepreneurs, officials, politicians, incorporating proposals and acting; with the capacity to intervene in key aspects of management (Alberqueque 1999).

Aligned to the idea that local development does not belong to any particular discipline, various technical and professional profiles can assume the leading and militant role in local development processes (Arocena, 2002, p. 137).

Martínez (2010) presents the actors in his development scheme as centrals, clarifying -in line with our observations, that there are certain points where development policies implemented by governments, should be careful in order to really benefit involved. He specifically states that: “The system of promotion of productive activity established, must consider as priority actors the local residents” (translated, Martinez, 2010, p11).

This seeks to ensure that the external human support introduced into the territory, is make after an exhaustive analysis of the limitations of the community. The intervention must have at exclusive and superior aim to improve opportunities for the inhabitants of the territory, and no facilitate the way for companies to invest in communities using low labour cost and taking profits.

Here again we agree with Martínez (2010), that the system should we be careful: if the social net is weak for the development of production projects, programmes should be designed for State intervention to correct this weakness in the ‘places of life’, in instead of replacing local actors by



outsiders, because these almost inexorably will be temporary (Sforzi, 2007, p. 36).

## **The Role of the State**

The role of the State as we advance is relevant and determinant in many cases; acts as a harmoniser and catalyst, articulating public and private plans of the actors.

The PEI, which reflects the current government official proposal for the coming years, expound that public investment made in infrastructure, education, technology and science since 2003, has led to significant progress; but the intention is to deepen that dynamic, incorporating local resources (human, natural and financial) in order to increase investment in the own territory, focussing the search for sustainable development (Ministerio de Industria, 2010).

In this plan 11 industrial production centres are rescued. The objective is to develop regional forums where workers, academics, businessmen, representatives of the Ministries of Finance, Industry and Federal Planning, provincial and municipal governments, meet in a space conducive to articulation of various sectors to realise the re-industrialisation.

This process is organised by working on value chains, composed by all necessary activities to produce a good from its initial conception to delivery to the final consumer. This system emphasises the dynamics of the relationships inter and intra sectorial of the economy.

Thus, the objective of PEI is to achieve competitiveness along each chain and in all productive chains. Specifically, it presents science as a crucial resource and with it an 'industrialisation of rurality' in terms of generating an industry upcoming to the location where the resources are generated, that reaches international standards of leadership increasing the competitiveness of the entire value chain (Ministerio de Industria, 2012, p. 273).

In our judgment, to improve the living conditions of a micro-region or small towns in the province of Buenos Aires, at present, the focus should be set on the local production and marketing of goods for use and consumption, pointing to the replacement of extralocal goods (Del Giorgio Solfa & Giroto, 2009).

## **The Role of Industrial Design**

In the context of local development, we conceive the figure of industrial designer in a central position with respect to the articulation between entrepreneurs and users, analysing specific needs, technological and human resources available in the territory, to capitalise efficiently in the design and development of new products (Dean, 2001).

In this case, the industrial designer will focus on executing the steps involved in the process of satisfying the needs of families, the same time as they focus on the replacement of goods produced in other regions of the country.

Along the way, it will connect various disciplines from the local productive system to final recipients of the market (Sierra, 2012).

In this sense, the industrial designer can be configured as an agent of change in productive enterprises, articulating the technical knowledge that will adapt in response to the dynamic needs of the local society (Alburquerque, 1999).

Also, the transfer of product design to entrepreneurs, will seek to promote the autonomy of the different actors, capitalising features of local identity (Garbarini, Delucchi, and Vazquez, 2010).

In these cases, the designer will have the role of identifying which are the regional characteristics that could be manifested in the morphological communication (symbolic), to enhance the products developed<sup>12</sup>.

It is further displayed the role of manager and organiser of the production system, where the contribution of the design focusses on facilitating technological processes undertake by small manufactures in their change of scale<sup>13</sup>.

## **The Role of Marketing**

The marketing dimension represented by different technicians and professionals in the field of management and economics, mainly will comprise two processes: 1. Analysis and diagnosis of: value chains; territorial resources; and cost structure and prices of extra local products. 2. Development of marketing plans for local products and services (Cipolla & Manzini, 2009).

The first process will focus on identifying opportunities for local economic development. Therefore, first the main productive chains of the territory will be analysed, selecting those with important processes outside the territory. In them, the external links feasible to be developed in the locally will be recognised.

We believe that the processes of buying goods are more inefficient when local prices exceed the actual prices excessively. In this logic, it will be taking into account the rising price involving no local transport of products.

Can also be identified opportunity among land resources, rescuing particularities of rural, urban and architectural landscape, which will be essential to recognise a potential tourist profile (Giroto & Del Giorgio Solfa, 2009).

In the role incumbent on the second process, in response to the projects generated in the framework of local development, it will be design and implement marketing plans to promote new or existing, local products and services (Simonato, 2009; Del Giorgio Solfa, 2012b).

Some of these strategies promotional product will be aimed at promoting the purchase of local products; others will point to the development of products and services channels –of local production– projected to expand the regional market (Cipolla & Manzini, 2009).

## **The Role of Entrepreneurs**

Though the local development approach will allow different actors to become entrepreneurs, can mainly consider two profiles: the social entrepreneur and the business entrepreneur.

The social entrepreneur is a charismatic leader with social acceptance, that committed to the idea of local development, will interact with the other actors adding followers and spreading the benefits and potentialities of the approach (Giordano, 2012).

Instead, the business entrepreneur, attentive to socioeconomic and productive needs, projects action and mobilises resources to generate new business assuming the risks involved<sup>14</sup>.

In this framework, entrepreneurs in the technology sector are an important perspective for new productive enterprises. Among them we have the technicals and professionals of the areas: agriculture, food, biology, construction, electrical, electro-mechanical, electronic, gastronomy, hospitality, industrial, mechanical, environmental, civil and water works, chemicals, tourism, etc. (Thomas, 2012).

Considering that most of the bonaerenses parties have secondary technical training institutions, they could play a fundamental role in the processes of local development, cooperating further in professional education, aligned to local productive enterprises (Narodowski, 2008).

In this context, then we understand that education can develop skills and contribute to the generation of business initiatives based on negotiation skills, leadership, new product development, creative thinking and technological innovation<sup>15</sup>.

## **Needs and Potentialities of Productive Chains**

In the towns of the province of Buenos Aires, there are needs for goods of use and consumption in reasonable qualities and prices (Quetglas, 2008). Specifically, in small towns that are distant, far from the metropolitan region.

On one hand, we understand that transportation and distribution of certain products manufactured in the Greater Buenos Aires, would produce a deficiency in the processes of acquisition and purchase of the residents of this kind of localities.

This deficiency lies essentially in the high transport costs assumed by the final price of the product, resulting in up to 100 percent more expensive (furnishings large size).

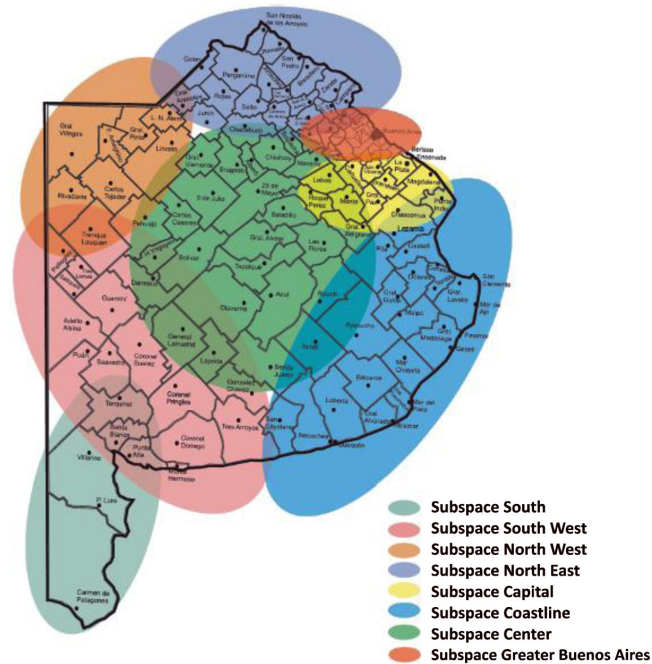
On the other hand, levels of development and innovation in such localities, remains paralysed because of the disarticulation of production systems initiated over two decades ago and whose effects result in lower development opportunities for communities, less employment and emigration to others most dynamic regions (Schorr, 2004).

In this reasoning, we found that the main potentialities are focus on those goods for use and consumption of low complexity that can be produced in the territory. There are a number of furniture goods and consumer products (food, cleaning chemicals), which can be produced or finished there<sup>16</sup>.

From a provincial perspective, analysing the bonaerenses productive chains, we found that some can be more or less competitive depending on the Sub-space where they are located.

From the provincial policy, the PEPBA highlights the value chains that can enhance local development and value addition at source.

To rate the needs and potentialities of the productive chains, we will take the classification of the PEPBA which, on the basis of the PEI, defines eight Subspaces (see Figure 7.1) and define in each of them the productive chains in which it will base its production plan.

**Figure 7.3: Subspaces Distribution**

Source: *Ministerio de la Producción, Ciencia y Tecnología* (2012, p. 9).

In these subspaces we find among 4 and 11 productive chains, which we will consider overall, although in this paper we focus on the needs and potentialities common to the type of locations that we aim (see Table 7.3).

It can be seen from the analysis of this table that the Buenos Aires production system is varied and displays important coexisting productive chains in its vast territory.

For certain productive chains, the chances of capitalising our comprehensive approach that includes design, marketing and entrepreneurship are greater than others, but in most cases, we found that the PEPBA promotes the incorporation of them in the ranging process of their local development objectives.

Table 7.3: Detail of Existing Productive Chains Existent in each Sub-space, their Needs and Potentialities	
Sub-space	Productive Chain
South	Petrochemical Complex; Onion; Oiler complex; Sheep.
South West	Wheat Flour Mill; Footwear Complex; Emerging Tourism; Apicultural complex; Barley.
North West	Oleaginous complex; Textiles; Corn and Poultry.
North Est	Metalworking Complex; Autoparts complex; Apicultural complex; Fruit.
Capital	Horticulture; Petrochemical Complex; Naval Complex; Software and Computer Services.
Coastline	Tourism; Incipient Dairy Complex; Clothes; Naval Complex; Software and Computer Services.
Centre	Cattle; Dairy; Swine; Cement; Agricultural Machinery.
Greater Buenos Aires	Footwear; Textiles and Clothing; Dairy; Automotive - Automotive parts; Agricultural Machinery; Capital Goods; Construction Materials; Software and Computer Services; Petrochemical Complex; Medicinal Products for Human Use; Industrial Forest.
<i>Source: Own elaboration based on data of Ministerio de la Producción, Ciencia y Tecnología (2012)</i>	

## Local and Human Scale Development

To deepen the local dimension, which we will define what we consider as local and human scale development.

The local scale is the establishment of a limit on the number of people living in the territory will be subject to development interventions, to consider it into our local scale (Arroyo, 2001).

It has been agreed that this population range should be between 5,000 and 30,000 inhabitants, based on criterion, which seeks cover municipalities with potential for territorial development, with important and balanced domestic consumption, whose progress is hampered by the proximity of parties with higher productive scale constituted as regional heads<sup>17</sup>.

Even though strategic plans evaluated, considered most relevant regions and productive chains, we will focus on local development programs based on the needs and potentialities common to such localities.

In this way, we consider key at Max-Neef, Elizalde, & Hopenhayn (1986) who define human scale development as: the sustained in the satisfaction of basic human needs, the generation of growing levels of self-reliance and organic articulation between: humans, nature and

technology; global processes with local behaviours; social with personal; planning with autonomy and civil society with the State.

Thus human needs, self-reliance and organic articulations constitute the fundamental pillars of human scale development (Max-Neef, et al, 1986, o.14).

The authors specify that for this type of development work, it must be based on a real prominence of people, to achieve the passage of person-object to person-subject where the main problem is the scale: there is no possibility of prominence in giant systems, hierarchically organised from top to bottom (Max-Neef, et al, 1986, o.14).

## **Conclusions and Proposals**

In the first instance, the review of the literature about local development, entrepreneurship, industrial design and marketing together with institutional inputs (strategic plans and mixed territorial resources) and the statistical information available, we can conclude that its feasible to integrate actions to contribute to local development. Context analysis allowed us to recognise a manufacturing vacuum in small populations, product of the disarticulations -of small and micro industries- in the 90s.

The focus in the province of Buenos Aires, took us to contextualise a type of territory starred by municipalities with great potential for local and sustainable development. And also, recognise, which are the natural, human and institutional resources that can support the endogenous development of these local territories.

Furthermore, understanding the roles of each of the disciplinary dimensions we suggest to integrate, we discovered in what degree each actor -individual and synergistically- can cooperate with implementation activities of local development projects.

In addition, the establishment of an appropriate scale of populations to design this type of local development strategies, together with the analysis of the potentialities – common endogenous and differential regional results were obtained, which allowed identifying some common objectives for local manufacturing (Thomas, 2012).

These targets, especially considered the development of use and consumption products for the home, based on production – of low complexity – of furniture (wood, melamine and upholstery), meat (especially pork) and chemical (bleach, detergent, soap), among others. These manufactures can (re)organised perfectly in local territories, employing more people and lowering prices (see Table 7.4).

<b>Table 7.4: Examples of Contributions of Industrial Design for each Dimension</b>			
	<b>Furniture</b>	<b>Food</b>	<b>Chemicals</b>
<b>Productive System</b>	<ul style="list-style-type: none"> <li>• Materials optimisation</li> <li>• Integration of carpentry, blacksmith and upholstery.</li> </ul>	<ul style="list-style-type: none"> <li>• Design of Implements for the primary and secondary production in low scale.</li> </ul>	<ul style="list-style-type: none"> <li>• Implements design for fractionation at low and medium-level.</li> </ul>
<b>Product</b>	<ul style="list-style-type: none"> <li>• Design of wood, melamine and upholstered products.</li> <li>• Self-assembly design.</li> </ul>	<ul style="list-style-type: none"> <li>• Design of new products based on consumer behaviour.</li> </ul>	<ul style="list-style-type: none"> <li>• Dispensers design for specific uses.</li> </ul>
<b>Packaging/ Container</b>	<ul style="list-style-type: none"> <li>• Reduced packaging.</li> <li>• Communication and assembly instructions.</li> </ul>	<ul style="list-style-type: none"> <li>• Communication of the quality, designation of origin and other qualities.</li> <li>• Additional benefits for consumption.</li> </ul>	<ul style="list-style-type: none"> <li>• Design of new packaging based on consumer behaviour.</li> </ul>
<b>Marketing</b>	<ul style="list-style-type: none"> <li>• Modular and personalized products.</li> <li>• Strengthening of the “buy local”.</li> </ul>	<ul style="list-style-type: none"> <li>• Development of the product portfolio.</li> <li>• Higher quality perceived by low production scale and proximity.</li> </ul>	<ul style="list-style-type: none"> <li>• Low prices.</li> <li>• Quality with local responsibility.</li> </ul>

In addition, other distinctive potentials were identified – according to the analysed regions-, resulting in sectors related to tourism, cultural industries, etc.

It is in these sectors and this kind of commodities of use and consumption, where the greatest potential exists, and where the disciplines of marketing, industrial design and entrepreneurship could act on behalf of the local and productive development.

It should be noted that the protagonists and/or recipients of local development not only benefit to getting products to more realistic prices, but will contribute to the creation of a more balanced territory in terms of employment opportunities, development and welfare. Therefore, this integrated design, marketing and entrepreneurship is key to local development in the province of Buenos Aires.

For an initial stage, local development agencies allow the organisation of entrepreneurial actions of territory and extra-local supports, coming from technological poles and nearest projects incubators. In this way, although not all municipalities have PT or incubators, they can capitalise somehow the state available resources.



In subsequent stages, should be established:

1. Survey of design and administration professionals
2. Presentation of local needs to the involved actors
3. Establishment of working groups for projects formulation and
4. Monitoring of the validated projects

With the purpose of improve the capabilities of local development for the bonaerenses territories and increase the quality of life of its inhabitants, is proposing to revalue these disciplinary fields and perform this proposal for immediate implementation.

Certainly, it is quite convincing that its worth assign resources to a policy of local development-based on design, marketing and entrepreneurship – in the province of Buenos Aires.

## Endnotes

- 1 The Strategic Industrial Plan 20 20 (*Plan Estratégico Industrial 20 20*) is a plan developed by the Ministry of Industry of Argentina. On it, eleven industrial productive centers are selected for being developed in regional forums compounds by: employers, workers, academics, ministries of Economy, Industry and Federal Planning, provincial governments and municipal governments. It is an institutional articulation between nation, provinces and municipalities, public institutions and NGOs. It is a collective project with key guidelines for the development of industrial sectors with perspectives until 2020.
- 2 Federal and Participative Agri-food and Agribusiness Strategic Plan 2010-2016 (*Plan Estratégico Agroalimentario y Agroindustrial Participativo y Federal 2010-2016*) is a plan developed by the Ministry of Agriculture, Livestock and Fisheries of Argentina, which aims to promote a shared vision for the agri-food and agribusiness related sectors. It proposes to establish long-term policies that generate predictable, stable rules and a collective national project through the involvement of the different social actors and building institutional capacities.
- 3 The Buenos Aires Productive Strategic Plan 2020 (*Plan Estratégico Productivo Buenos Aires 2020*) is a plan elaborated by the Ministry of Production, Science and Technology of the Province of Buenos Aires. It provides the basis for develop human resources and infrastructure, to make possible the objectives of PEI 20 20 at the provincial level; by describing and analysing the existing productive chains in the eight sub-areas strategically defined.
- 4 The National Plan for Local Development and Social Economy 'Let's get to work' (*Plan Nacional de Desarrollo Local y Economía Social Manos a la Obra*) is a public policy promoted by the Ministry of Social Development of Argentina, to promote social economy through technical and financial support to productive enterprises for social inclusion that are generated within the framework of local development.
- 5 Ministerio de Agricultura, Ganadería y Pesca, 2010
- 6 Ministerio de Trabajo, Empleo y Seguridad Social, 2014
- 7 García-Tabuenca, Crespo-Espert, & Cuadrado-Roura, 2011; Ministerio de la Producción, Ciencia y Tecnología, 2012
- 8 Narodowski, 2008; Kotsemir, Abroskin, and Meissner, 2013
- 9 Arocena, 2002; Rodríguez, 2006; Del Giorgio Solfa, 2012
- 10 Del Giorgio Solfa, 2012
- 11 Moalosi, Popovic, & Hickling-Hudson, 2007; Li, Su, & Huang, 2008
- 12 Chang, Wysk, & Wang, 2006; Aguilar-Zambrano & Hernández-Romero, 2012
- 13 Spadafora, Barbieri, Cajade, Bonano, & La Rocca, 2010
- 14 Gunes, 2012; Zappe, Hochstedt, Kisenwether, & Shartrand, 2013
- 15 Okudan, Ma, Chiu, & Lin, 2013
- 16 Arroyo, 2001; Del Giorgio Solfa & Girotto, 2009
- 17 *Ibid*

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Section II:

# Competition for Inclusive Economic Growth

Designing competition reforms in developing and least developed countries to better contribute to inclusive economic growth, especially by creating greater scope for Micro, Small & Medium Enterprises (MSMEs)





## 8

# The Theory of Competition and ‘the Developmental State’ in Africa

## *A Case Study of Kenya and South Africa*

PAUL KINYUA  
*Lecturer, Catholic University of Eastern Africa  
Nairobi, Kenya*

### Abstract

Kenya embarked on policy reforms relating to competition law since the early 1980s. The paper takes a ‘political economy’ perspective to assess the policy outlook and economic choices entailed in the legal framework of competition law in Kenya. ‘Political economy’ is defined as a discipline within the social sciences that is concerned mainly with the nature and causes of the wealth of the nation and its distribution to different sections of society. Kenya, in East Africa, provides a feasible testing-ground for the theoretical claims of different schools of thought concerned with competition policy in particular and political economy more generally. The paper examines the points of convergence and divergence between the overarching national policy to foster ‘development’ on the one hand, and the specific policy choices relating to competition law and the institutional practice of competition authorities in Kenya on the other. The main argument of the research is that while Kenya’s national economic policy outlook took a turn to the right in the early 1980s, with a de-emphasis of the role of the State to spur development, the laws and policies to regulate competition in Kenya appear more suited to mixed-economy environment rather than to an unfettered free-market regime. The paper concludes that, of the countries examined, South Africa offers Kenya the most illustrative example with regard to the design and implementation

of a competition policy well-attuned to the broader vision of the national economy.

## **The African Context of Competition Law**

Political independence was attained by the majority of African countries in the 1960s and 70s.<sup>1</sup> The attainment of sovereignty, however, has not led to the economic transformation of these countries. The historical period beginning in the 1980s marks the beginning of the ascendancy of neo-classical economics in Africa Zeleza: 1996. During the 1960s and 1970s, State-led development was seen as the best way of promoting the economic development of Africa.

The triumph of neo-liberalism in Africa was facilitated by the perceived failure of Keynesianism in developed countries, the failure of 'developmentalism' in developing countries, and by the collapse of the Soviet bloc<sup>2</sup>. Privatisation' and 'Deregulation' became the major pursuit by global capital in the drive to penetrate the markets of developing countries.

African economies are disarticulated in the sense there are few forward or backward linkages between the commodity-exports sector and other sectors of the economy. In these respects, sub-Saharan African countries in general are comparable with each other. African economies lack a capital goods sector of any note and rely on imports of heavy machinery and vehicles. Africa remains highly reliant on foreign investment, particularly from the former colonising countries; and looks to the latter countries as the primary source markets for external trade, tourism, loans and foreign aid.

The structural weaknesses of the African State have been attributed to a host of causes. Ademujobi and Olukoshi identify two major challenges faced by African countries in general.<sup>3</sup> First, is their overdependence on the external world, and second is the under-exploitation of their development potentials at the national, regional and continental levels.<sup>4</sup>

Africa's principal challenge in the twenty-first century is how to design and implement effective policies to promote industrialisation and economic transformation. In the 21st century, African countries are integrated into the world economic system mainly as importers of finished products and exporters of primary products and raw materials.

African countries often rely on multinational corporations (MNCs) as agents for technological transfer and economic development<sup>5</sup>. Technology, manufactured goods and technical know-how have, however,

been imported at prices way above those earned from exports, creating a situation of unequal exchange between Africa and the world market.<sup>6</sup>

Neo-liberal economic theory considers the security of property rights to be of paramount importance for the functioning of an efficient market; however, the efficiency of the market is said not to be dependent on the distribution of property rights (Froneman: 2007: 216). Similarly, the distribution of income produced by the market is not an economic concern, but a political one (Froneman: 216). Those that argue that efficiency is the only aim of competition policy insist that competition authorities should intervene only when an anti-competitive practice has been committed and is detected.<sup>7</sup>

In opposition to this view, one main argument from the literature on 'market failure' is that the government must establish public enterprises to ensure that the public interest is catered for (Aseto & Okelo: 1997: 7). Public enterprises under government control are meant to maximise social welfare, and improve on the decisions of private enterprises when monopoly power or externalities introduce divergence between private and social objectives (Aseto & Okelo: 8).

For a market to function properly there must be competition and also regulation of those monopolies that exist, whether these belong to the public or the private sector (Nove: 1992: 48).

Biersteker provides three justifications for State intervention in markets from a 'political-economy' point of view (Biersteker: 1992).

Firstly, the State could intervene to correct a market failure. The market fails on its own when the prices of goods and services give false signals about their real value, confounding communication between producers and consumers (Aseto & Okelo: 1997: 7).

Secondly, the government could intervene to provide a genuine public good. Thirdly, State intervention could be justified on the ground that it is necessary for the State to take control of the 'commanding heights' of the economy to ensure provision of a greater public good.

Antitrust laws have been applied against two types of combinations: the first type is the so-called 'close-knit combination' that is formed by trust, holding company, merger or consolidation. The second type is the 'loose-knit combination' which refers to (restrictive) agreements among individual competitors to, for instance, fix prices (Stelzer: 1986: 107).

The main goals of competition policy include: (1) to promote economic efficiency through a proper functioning of markets; (2) to ensure equity; and, (3) to control the economic and political power of big business.

Different writers, however, disagree on which of the objectives listed above or their combinations should be the subject of competition policy.

Mehta, for example, appears not to lend support to the position that ‘efficiency’ should be the only goal of competition policy. He argues that “although efficiency has been a central role of antitrust, it should not be the only one” (Mehta: 2013: xxxii).

The drive to enact competition laws in African countries has been taking root steadily since the mid-1980s. Competition laws passed by many African countries have attracted the criticism that they could be unresponsive to local needs and conditions:

Competition laws in most developing and third world countries ...are mostly fashioned after the existing legislation originating from the European Union (EU) or the United States of America (USA). While a lot of these pieces of legislation are often modified to suit the needs of these developing countries, it is usually not the case that a cautious approach is taken to ensure that imported legislation is designed to meet the specific national challenges in Africa (Adeleke: 2011: 5).

This paper addresses the general context of competition law in Africa from a ‘political economy’ perspective and is grounded on the economic history of Africa between 1900 and 2015. ‘Political economy’ is a discipline within the social sciences that is concerned with the nature and causes of the wealth of the nation and its distribution to different sections of society. For the classical political economists including Adam Smith, David Ricardo, John Stuart Mill and Karl Marx, political economy was a science defined by its subject matter, i.e. the ‘science of the economy’, and the economy itself was treated as part of a much wider social context.

Part I of the paper outlines the social, political, and economic context of Africa roughly between the years 1900 and 2015. Part II gives the historical background to competition policy and law by revisiting the emergence of the anti-trust movements in the United States of America in the 1890s. In part III below, the basic arguments of competition theory, which are derived from neo-classical economics, are critically examined and the ascendancy of neo-liberal economics in Africa since the 1990s is re-visited.

Part IV of the paper defends its case that Kenya and South Africa are fit for a comparative examination and concludes the paper. The paper focusses on the economic structures established during the period of colonial (including apartheid) rule in Kenya (1895-1963) and South Africa (1867-1994).

Two questions are posed in the paper concerning the general context of competition law in Africa: the first question is: what are ‘the established hierarchies’ of the national economy of Kenya and South Africa? This question touches on the mode of integration of African countries into the

world capitalist system in the opening decades of the 20th century. The second question asks: ‘in whose interests does the national economy of a given African country function’<sup>8</sup>?

Dumont submits that it is impossible to conduct an action in the economic sphere without political repercussions (Dumont: 1968: 169). He concludes that one cannot attain ‘development’ for an African country by remaining apolitical; such an attitude, in his view, could only be hypocritical (Dumont: 169).

## The Political Economy of Contemporary Africa

The ‘commodity boom’ that held so much promise for African exports in the world market since had already begun to fade out by the year 2011. The Economic Commission for Africa (ECA) noted in its 2013 report:

Since 2000 the continent has seen a prolonged commodity boom and sustained growth trend. And although growth slowed from an average of 5.6 percent in 2002-2008 to 2.2 percent in 2009 – hit by the global financial crisis and steep food and fuel price rises – Africa quickly recovered with growth of 4.6 percent in 2010. The continent’s growth slipped again in 2011 owing to political transition in North Africa (ECA: 2013: 6).

Although Africa registered strong growth at about 5.0 percent in 2012, in early 2016 oil prices fell to their lowest since 2004, clearly pointing to a steady leveling off of the ‘commodity boom’ that has lasted for slightly more than a decade.

This section locates Africa within the international political economy. It retraces the integration of African countries as peripheries, and later as semi-peripheries of the world capitalist system in the last decades of the 19th century (Mikell: 1989). It draws mostly from writers belonging to the critical school in international relations (IR) discourse, especially the work of Robert Cox and Branwen G Jones.

To develop an understanding of the world economy as an analytical category, this research draws on the history of the rise of capitalism in Western Europe in the fifteenth century, the development of western capitalism throughout ‘the long 16th century’, the transformation of capitalism from a *competitive* phase to a *monopoly* phase in the late nineteenth century, and the spread of industrial-finance capitalism to Africa, through the vehicle of imperialism, during the last three decades of the 19th century.

Chanock observes that the failures of the States created by colonialism, and their powerlessness in relation to the goals of development can be directly linked to “the structure and workings of the world economy”

(Chanock: 2002: 44) Zeleza categorises the contending positions on African economic and social history between 1950 and the mid-1990s into seven major schools of thought: (i) 'nationalist and liberal narratives' (ii) 'orthodox development theory' (iii) 'classical Marxist theory' (iv) 'Raul Prebisch (ECLA)' (v) 'unequal exchange' (vi) 'dependency theory' and (vii) 'successful capitalism in the periphery' (Zeleza: 1996).

It is not possible to summarise this vast literature in this contribution. These theories on the political economy of contemporary Africa can be grouped simply into two: (a) theories that emphasise the 'structural causes' of Africa's marginal position in the world economy on the one hand: (iv, v, vi in the list above); and (b) theories that focus on the 'agency' of African countries to attain industrialisation, on the other hand: (i, ii, iii, vii in the list).

Competition cannot be adequately understood without appreciating the process of accumulation and reproduction of capital in any given 'national market' and within the world economy.<sup>9</sup> Capital accumulation originates in the production of commodities which embody both use value and exchange value (money) (Mandel: 1995: 6).

Cox describes the emergence of capitalism, its spread and the emergence of capitalism's 'monopolist phase'.

Capitalist development is a process that was put together gradually over a period of some five centuries, beginning in western Europe from the 14th century before it became, in the nineteenth, a coherent expansive force on a world scale. This expansive force at the mid-nineteenth century point was in a competitive phase. From the late 19th century, capitalist development entered a new, monopolistic phase (Cox: 1987: 51).

In capitalist societies, the State's regulation of competition between individual capitalists invites disputes within the dominant classes, whose cohesion is a pre-condition for their domination over the rest of society (Berman & Lonsdale: 1997: 79). Reproduction of capital, Marx explains, is the unity of the process of production and the process of circulation (Mandel: 60).

Money is the epitome of human self-alienation under capitalism, since it reduces all human qualities to quantitative values of exchange (Giddens: 1971: 214). Due to the ever-present class-conflict in the surrounding society, Berman and Lonsdale insist, every capitalist State must necessarily be involved in 'a process of abstraction'<sup>10</sup>.

In order to maintain its own legitimacy – the state must be seen to act on behalf of the social order as a whole... the twin functions of guaranteeing the technical and legal conditions of capital that competition

cannot provide – monetary and tariff rules, property laws and so on – and of maintaining the hierarchy of class domination have both been abstracted from the economic to the political sphere within each national social order<sup>11</sup>.

The crisis of legitimacy experienced by many African States has given currency to the argument that the unitary structure is unsuitable to African socio-cultural conditions. However, this leads to a more disturbing question, should African countries and peoples do away with the whole idea of the State? According to Mafeje, taking into consideration Africa's vulnerability to the forces of globalisation, it would not be in Africa's interests to abandon the State form, because the State is the most important single actor in the political and economic arena in Africa (Mafeje: 2002: 78).

Beckman observes that what neo-liberal ideology wishes to prevent from being realised with its prescriptions of 'privatisation' and 'deregulation' is the 'economic nationalism' of developing countries:

In an effort to delegitimise the principal ideological rival [which is] economic nationalism- neoliberals seek to delegitimise the State, the main locus of nationalist aspirations and resistance to the neoliberal project. In order to undercut the claims by the State to represent the nation, its alien nature is emphasised. Its retrogressiveness is explained in terms of (detachment from) civil society... rent-seeking, patrimonialism and autonomy (Beckman: 1998: 46).

The contestation between global business and developing countries more generally has witnessed the USA acting as the leading advocate for reform, by pushing other countries to deregulate their financial markets (Greider: 1997: 33).

Deregulation includes the following strategies: relaxation of controls on capital inflows and outflows, 'flexibility' of labour and environmental laws, removal of interest rate controls and removal of taxes on currency-exchange transactions. Writing in 1997, Greider noted that 'transnational commerce' had "aggressively campaigned over three or four decades to free itself from various social controls imposed by ... governments" (Greider: 33).

Global capital has also tried to penetrate developing countries' market through bilateral investment treaties (BITs) signed between developed and developing countries. The profusion of BITs since the mid-1990s has brought to the fore issues touching upon States' sovereign decision making authority, States' accountability to their respective populations and the State's unique role as guardians of the public interest<sup>12</sup>.

The general tenor of recent BITs is that they are primarily instruments to constrain the sovereign power of home governments to interfere with investor property. What is more, some constitutive agreements of the World Trading Organisation (WTO), such the TRIPS Agreement, appear to have been designed with the interests of global capital as their primary theme of focus. It is submitted that the international economic and political context that Africa encounters during the second decade of the twenty-first century is as important as the national economy and that both contexts should inform the choice of 'goals' to be served by competition law in African countries.

Some economic historians and scholars trace the emergence of a functioning 'world economy' to the late nineteenth century, (MacMillan: 1996) while others point to the 18th century, and even earlier.<sup>13</sup> Strachey, for example, notes that between the years 1815 and 1870, the "well-organised, large-scale British trading corporations" of that period had an immense bargaining power against "disorganised peasant societies even without acquiring sovereignty over them" (Strachey: 1959: 73; Keynes: 1920).

In these circumstances, he concludes, an 'anti-imperialist climate of opinion' was formed in Britain (Strachey: 72-3). Robinson and Gallagher describe British relations with Africa during the last 50 years of the 19th century as conforming to their brief formulation: "informal empire where possible, formal empire if necessary"<sup>14</sup>. Although this appealing summing up is not entirely inappropriate, their main thesis that 'monopoly capitalism' did not drive the imperialist annexation of Africa in the late 19th century remains intensely contested.<sup>15</sup>

The main thesis of the economic imperialism argument is that capitalism, upon reaching the monopoly stage of the trusts in the last three decades of the nineteenth century called for imperialism. The period between the Universal Exhibition of 1851 where Britain, then the world leader in industry exhibited the latest equipment and products to a largely pre-industrial European and North American audience, and the year 1866, is seen as the highest point of the liberal era (Cox: 1987: 151). The 1870s oversaw the decline of liberal free trade policies in Europe and the rise of a new imperialist era.

Late nineteenth century imperialism captured Africa for the world capitalist system and transformed Africa's pre-capitalist relations of production to "part-economies, externally oriented to suit the dynamic of a capitalism that had been imposed upon them from outside" (Berman & Lonsdale: 78). Although Lenin is often grouped together with Hobson, Hilferding, and others who argue that 1880s imperialism resulted



from the transition of capitalism to a monopoly phase, Stokes insists that: “[on] the vital question of chronology Lenin made it plain that the era of monopoly finance capitalism did not coincide with the scramble for colonies between 1870 and 1900 but came after it” (Stokes: 1969: 285).

Strachey’s book, written at the sunset stages of the British Empire in 1959, is meant to dissuade the public in Britain and United States from running an empire. He discouraged enthusiasts of empire in the several political parties that he claimed allegiance to throughout his long political career from the continuation of British colonialism into the latter decades of the twentieth century.<sup>16</sup> Strachey wrote that the primary motives behind British imperialism were capitalistic in nature:

[T]o turn the terms of trade in our i.e. British favour was not the characteristic purpose of the intensified imperialism, which set in after 1870. Its main purpose was rather to secure fields of investment for the surplus capital, which could not be so profitably invested at home, given the existing distribution of the national income. And the successful achievement of massive foreign investment, and of the imperialism that went with it, immediately enriched, not the British people, but a narrow class of investors (Strachey: 1959: 154).

Although he arrived at this conclusion, Strachey made the following claim: “there is no evidence that Britain’s imperial possessions enabled her to enrich herself by turning the terms of trade in her favour” (Strachey: 148).

Strachey’s observation amounts to saying that empire was not a net gain for Britain but a balanced sum with benefits and losses oscillating more or less equally between Britain and the colonies during the history of imperialism.

It is to be wondered whether that actually was the case with respect to British colonialism. Strachey defined terms of trade ‘from the British point of view’ as: “the ratio of the prices of our imports and exports... the terms of trade are said to have become more favourable to Britain when the prices of the things she sells have, on the average, gone up and the prices of the things she buys have gone down (148)”.

Even accepting Strachey’s conclusion that Britain did not benefit more economically than the colonies which were under British tutelage throughout the life-span of the empire, this apparently technical conclusion would need to be counterbalanced by the observation that imperialism need not benefit the whole British nation.

It is important to recall, as indeed Strachey himself found, that a narrow class of capitalist ‘investors’ did derive massive economic gain from imperialism. If then this is the case, has not imperialism done its bidding?

It may be asked, in response to Strachey, can one genuinely claim that the books are evenly-balanced between Britain and her African subjects in colonial Kenya, South Africa or Zimbabwe just because the vast majority of British citizens did not partake a share in the theft commissioned by the Cecil Rhodes and Captain E S Grogans of imperial tradition, who gained huge financial windfalls from brazen seizure of African lands and commandeering of African mineral wealth?

Strachey ought to have interrogated his data more deeply than to have adopted it in one long leap. Britain's 'terms of trade' during the imperial period need to be inspected carefully beneath the general form, or veneer, in which international trade data is officially recorded.

Extending Strachey's system of imperial book-keeping to the Congo Free State, and proceeding thereupon to ask oneself how the balance fell between Belgium and the Congo Free State during King Leopold's reign, leads to very interesting destinations. Imperialism was of benefit to some actors; in particular, it benefitted individuals, mostly white men and their progeny, and corporate entities.

Perhaps of equal importance to 'whether monopoly capitalism led to imperialism in the closing decades of the nineteenth century' is the economic effect of the colonial legacy in Africa. Magubane points out one key difference to be observed between the development of capitalism in Western European countries such Britain compared to the African periphery. In his view, in the capitalist societies of Western Europe, the working classes (proletariat) managed to break away completely from the subsistence economy with the onset of industrial capitalism in the 19th century.<sup>17</sup> This was not the case in colonial Africa, Magubane insists:

In Africa, on the other hand, because of the traditional system of land tenure and because of the extractive nature of colonial capitalism, the integration of African peasants into the world capitalist system was marginal. It led to impoverishment without complete proletarianisation.<sup>18</sup>

In the colonial period, Magubane emphasises, African migrant labourers were not allowed to break away completely from the "tribal" social environment (183). This situation was based on the rationalisation, which assumed that African cities and towns, and commerce in these urban areas, were for 'whites only' (183).

Magubane's 'colonial capitalist mode of production' (CCMP) concept coheres with Basil Davidson's characterisation of colonial capitalism as having a 'dual character'<sup>19</sup>.

Brett would also seem to support this position where he argues that since the colonial government policy supported British firms in Kenya,

Uganda and Tanzania, Africans were denied the opportunity to accumulate capital through entrepreneurship. He concludes that colonialism laid the foundation for Africa's future dependence on the multinational corporation for the capital and skills required if industrialisation was to advance:

"An alternative strategy based upon the attempt to establish small-scale industry using technology which could be managed by members of the indigenous population would probably have taken longer to mature, but would not have had the negative effects so clearly visible in the present situation."<sup>20</sup>

Before the effects of the Second World War brought about a change in industrial policy for the colonies, official and unofficial circles in Britain continued to believe that primary commodity production provided the only really viable base for colonial development (Berman: 1990: 178). Up to the mid-1930s British firms opposed the development of competitive manufacturing in the Empire (Berman: 178).

In 1939, it was recommended that certain industries be established in British colonies (such as Kenya) to reduce their reliance on imports (Nyong'o: 1992: 11). African colonialism was extractive in nature and left behind structures, institutions and infrastructure designed to benefit non-Africans<sup>21</sup>.

Nyong'o gives three reasons why industrialisation did not take root in the colonies: Firstly, very few industries were established and even these were scattered. Secondly, colonial industries were aimed at serving tiny markets, mainly the settler communities, or else to produce certain commodities in the colonies during the war. Thirdly, industrialisation in the colonies did not aim to establish long-term projects that would eventually culminate in the development of a capital goods sector (Nyong'o: 10).

Import-substitution industrialisation (ISI) strategies were initiated in the 1960s and 70s and were characterised by massive public investment and ownership of enterprises and financial institutions. This period saw a major expansion of the State in the economy throughout the developing world. The State influenced, regulated, planned, mediated, distributed, and even produced goods and services (Biersteker: 200).

The basis for State intervention in Africa was necessitated by the colonial legacy of underdevelopment. The State as the pre-eminent institutional organisation in society was involved in the process of accumulation and reproduction of capital.

Africa's State system is a legacy of European colonisation; a despotic and exploitative system of governance supposedly adapted and changed for the better with independence (xii).

The hallmarks of the African State include: ethno-political fragmentation, patron-client relations between political elites and the people, dependency, and underdevelopment. These asocial characteristics of African States are the result of processes of political socialisation dating from the colonial era that alienates rulers from the ruled<sup>22</sup>.

Some critics have argued that Africa's pioneering nationalists in the 1950s should have understood that nation-states fashioned from the structures and relationships of colonial States and thereby produced from European and not African history were bound to be heading for trouble<sup>23</sup>. African independence governments have had to manage divided communities created by arbitrary colonial borders with varying success.

The independent State, Nyerere argued, had the twin tasks of development and nation building (Nyerere: 1967). The State preceded the nation. According to Bujra and Lando, the factors that led African countries to embrace authoritarian single party rule and military dictatorship in the late 1960s continue to condition African politics and have made it difficult for African polities to cohere.

The inability of many African States to consolidate democratic governance or even simply to create some form of stable political order invites a range of questions. First, it might be asked, what are the reasons for the chronic crisis of legitimacy affecting the State in Africa (Bujra & Lando: 2010: xii)?

Secondly, what has led to the failure of formal political institutions and the widespread exclusion of substantive groups from power in Africa (Bujra & Lando: xii)?

In East Africa, Tanzania proved a more cohesive nation compared to Kenya and this is usually attributed to the late Julius Nyerere's quality of leadership.

According to Founou-Tchigoua, the new African elites that assumed power with the attainment of independence inherited "the crisis of the post-colonial model that had exhausted its potential for expansion and had consequently brought about budget and trade deficits that could not be managed without massive foreign aid"<sup>24</sup>.

This crisis of macro-economic management was followed by the general crisis of capitalistic expansion in the industrialised countries and the disorganisation of the international monetary system caused by the unilateral decision of the USA in 1971 to withdraw from the Bretton woods institutions' monetary system, which was based on fixed but adjustable interest rates, and also based on the latitude given to States to control movement of capital<sup>25</sup>.

Private banks had free rein to lend credits to countries in the global South, and this triggered off an international and regional financial crisis<sup>26</sup>. Petro-dollars accumulated by international banks during the 1973 oil crisis were off loaded to developing countries in the form of cheap loans (Shivji: 2007: 16).

Although the oil weapon strengthened the diplomatic bargaining power of oil-rich African States such as Algeria, Libya and Nigeria in the 1970s and enabled Angola to survive a costly civil war, it seriously disadvantaged non-oil countries, such as Kenya, which faced increases in prices of petroleum products and manufactured products amounting to three or four times their pre-1973 levels<sup>27</sup>. By the end of the 1970s, cheap loans had turned into heavy debt burdens as the limits of the early growth experienced throughout the 1960s were reached.

Generally speaking, no African country had an economic base that could enable it to avoid falling into the “debt trap”.<sup>28</sup> The Cold War helped African leaders, such as Kaunda, Mobutu, Moi, and Mugabe attract a disproportionate share of aid, notwithstanding poor policy regimes, and to strengthen their hold on power by playing geo-politics<sup>29</sup>.

### **Privatisation, Deregulation and State Intervention in Africa (1980-2015)**

Africa’s industrialisation strategies after independence were designed to reverse the effects of the colonial legacy and thus to achieve ‘development’. Regrettably, the ISI strategies upon which Africa was to industrialise were for the greater part externally-generated. More importantly, some African governments lacked the managerial and financial capacity to operate public enterprises and financial institutions<sup>30</sup>. ISI strategies did not bear fruit in Africa, unlike in East Asia, leading to mounting and unsustainable deficits, stagflation and debt crises in many countries by the end of the 1970s (ECA: 2013: 8).

Per capita growth rates in GDP for all developing countries declined from an annual average of 3.4 percent between 1965 and 1980 to 2.3 percent between 1980 and 1989 (Grindle). For sub-Saharan Africa the average was -2.2 percent, hence the claim that the 1980s were a ‘lost decade’ insofar as the economic growth of African countries is concerned. In the 1980s African countries adopted structural adjustment programmes (SAPs), which forced them to de-industrialise. The theoretical bases of the SAPs was that the market was efficient and government interventions inefficient.

Consequently, long-term development planning was abandoned and industrial policies neglected in most African countries (ECA: 8). SAPs had a two-pronged strategy for African development. Firstly, the State would be 'rolled back' from its involvement in the economy by privatising public enterprises and confining the State to its traditional role as regulator. Secondly, even as a regulator, the State would be bound to act within the framework of the rule of law rather than through authoritarian commands (Nyong'o: 2002: 25). There was a shift from development strategies that were State-led to strategies that placed greater emphasis on market forces to generate economic growth (Grindle: 1996).

In the 1990s, three senior International Monetary Fund (IMF) officials gave eight requirements for the raising of the rate of private investment, productivity and growth in Africa.<sup>31</sup> These are (1) maintenance of a stable macro-economic environment; (2) far-reaching improvements in governance to avoid interference with private activity and to develop and maintain a transparent and stable legal and regulatory environment that reduces risks faced by domestic and foreign investors; (3) trade liberalisation; (4) privatisation; (5) civil service reform; (6) banking reform; (7) liberalisation of the agricultural sector; and (8) improving labour market flexibility and competitiveness.

The argument for privatisation of publicly-owned firms finds justification from at least two main approaches: one approach focuses on the concept of utility maximisation behaviour of property-owners (principals) and the managers of their property (agents). It argues that because both the principals and agents of every enterprise wish to maximise profit, subject to the information available to them during their decision-making, the decisions made by the totality of firms in the market can only result in allocative efficiency for the entire market.

The second argument for privatisation is the so-called 'public-choice theory'. It involves a political game between the public, politicians, bureaucrats, and managers of public and private enterprises. Public-choice theorists argue that each of these groups have their own distinct utility functions which they seek to maximise; however, these groups do not have access to identical information.

Public-choice theory argues that in democratic societies, the partial information held by these groups and the divergent interests they pursue will result ultimately in internal inefficiencies of publicly-owned enterprises. Public-choice theory asserts that managers of publicly-owned enterprises will tend to form coalitions with politicians and bureaucrats to secure higher pay, greater power and prestige. It is claimed that such is

not the case for private sector managers who must ensure that their firms remain profitable to enjoy similar pay, power and prestige.

Politicians, it is claimed, may find it to their advantage to set prices of publicly-owned enterprises at below marginal cost so that their chances of electoral success are enhanced. Thus the economic efficiency of public firms could be sacrificed where it does not improve the electoral prospects of political leaders.

Bureaucrats, for their part, are claimed to be primarily interested in increasing their departmental budgets to the largest extent possible in order to obtain pay-offs (rent-seeking behaviour). Public-choice theorists submit that the power and welfare of government ministers is naturally linked to that of bureaucrats working under them, and that coalitions between managers, politicians and bureaucrats will ordinarily result in the internal inefficiency of public firms.

Public choice theory rests on the assumption of methodological individualism (Nove: 43). Like neo-liberal economics, public choice theory disregards the complexities of human motivation and their effect on quality of performance by assuming ‘maximisation’ of personal utility or profit (43).

The counter-theory to privatisation and deregulation can be traced to the classical political economists including Smith and Marx but also to 20th century economists such as Baran, Keynes, and Gerchenkron. Smith noted that public authorities have a role to “erect and maintain certain public works and public institutions which it can never be in the interest of any individual ... to erect and maintain” (Smith: 1776).

## **The Origins of Competition Law: A Brief History the Antitrust Movement in the US**

From the 1890s the landscape of the ‘economic system of the West’, as Sampson calls it, was progressively dominated by large-scale enterprises (Sampson: 49). From the middle of the 19th century certain developments in transport, storage and telecommunications had paved way for the creation of a more integrated international economy (Jenkins: 1987: 4).

The latter half of the 19th century oversaw a phenomenon that some historians describe as the ‘industrial revolution’ (Gay & Webb: 1976). There was rapid development of railways, iron steam shipping, refrigeration and temperature-cooling techniques, and the invention of the telegraph (Jenkins: 1987: 4). Importantly, the third quarter of the 19th century saw the superseding of ‘competitive’ capitalism by ‘monopoly’ capitalism’ (Magubane: 1976: 176).

In the United States, for example, what began as a highly competitive oil industry with a large number of firms in the 1850s, came to be dominated by Rockefeller's Standard oil Trust during the last quarter of the 19th century (Jenkins: 51-2).

Chandler's historical study of the changing structure of 'the American industrial enterprise' emphasises the rise of 'new administrative needs' in the 1890s; resulting, in his view, from an increase in output by firms that less twenty years before in the 1870s were concerned only with manufacturing (Chandler: 1962: 24).

Chandler observes that following the depression of the 1880s and early 1890s, the US economy experienced the rise of 'the great impersonal corporations' which, "besides manufacturing goods, sold them directly to retailers or even to the ultimate consumer, and purchased or even produced their own essential materials and other supplies" (Chandler: 25).

The currently fashionable phrase 'global value chains', although not invented in the 1890s, adequately captures the structural integration of these multi-departmental enterprises, administered by full-time professional managers rather by small family groups (Chandler 24).

The Sherman Anti-trust Act was passed in 1890; it marks the beginning of the 'anti-trust movement' and had no counterpart in Europe at a similar time (Sampson: 1975: 44).

The originator of the bill that later became the Sherman Act, Senator John Sherman, stated that it was motivated by a need to "declare unlawful, trusts and combinations in restraint of trade and production" (Sampson: 44).

The Sherman Act was specifically designed to break-up the monopoly of *Standard Oil of New Jersey* which had dominated the oil industry in the USA for more than thirty years, as Sampson explains:

The anti-trust movement ... was supported not only by the theory of free enterprise but also by a faith in the power of the individual against organisations. The trust-busters saw themselves as defending the very core of democracy... (T)hey would turn on the oil companies as the symbols of everything that was sinister and secretive in modern industrial society (Sampson: 49).

The Sherman Act "was the first major counter-attack by the US federal government against corporate monopoly" represented by the large-scale trusts (Sampson: 50). The court in *Standard Oil Company of New Jersey v. United States* clarified that what the Sherman Act was meant to break was the unification of power and control not as a result of normal methods



of industrial development, but by new means of combination which were resorted to ... with the purpose of excluding others from the trade and thus centralising in the combination a perpetual control of the movements of ... products in the channels of interstate commerce<sup>32</sup>.

In *United States v United States Steel Corporation* (1920),<sup>33</sup> the question whether the “mere size” of a corporation could be considered as violating the objects of the Sherman Act was considered by the court. Both the majority decision and the dissenting opinion in *United States Steel* were in agreement that the mere power or size of a corporation itself did not offend the Sherman Act. The dissent by Justice Day captures the intent of the Sherman Act on the question:

The (Sherman Act) was framed in the belief that attempted or accomplished monopolisation, or combinations, which suppress free competition, were hurtful to the public interest, and that a restoration of competitive conditions would benefit the public (Stelzer: 19).

One basic difference between EU and USA competition policy can be noted: in the USA dominant firms might defend their anti-competitive conduct on grounds that such conduct did not result in any harm to consumers. American courts have tended to concentrate on conduct whose effect directly restrains output or increases price, to the immediate detriment of consumers, and to disregard as not constituting anti-competitive conduct those practices that do not directly cause such effect.

In the EU, on the other hand, the protection of competition as an institution is regarded as a principal objective of competition law. This being the case, anti-competitive conduct could not be excused in the EU on the reasoning that consumer welfare was not thereby harmed. There is a tendency in the EU to protect the structure of competition in the market rather than protect against losses to consumer welfare in the short-term (Soames:20).

In the EU, a competitive market is theorised to have long-run benefits. The basic assumption in the EU’s approach seems to be that harm to the competitive process will indirectly cause anti-competitive harm. In comparison to US courts, the European Commission (EC) has been more willing to assume harm based on potential adverse effects to the competitive process<sup>34</sup>.

With such fundamental differences in approach between the EU and the USA on how to ensure markets remain competitive, developing countries cannot be expected to adopt either the USA or the EU competition law frameworks without self-examination.

It bears emphasis that there is no universally-accepted definition of ‘anti-competitive conduct’. According to Sutherland, anti-competitive

conduct is merely that which a particular community regards as undesirable conduct in the context of commercial competition<sup>35</sup>.

Kenya's national economic policy outlook took a turn to the right in the 1980s, with a de-emphasis of the role of the State to spur development. Kenya introduced Structural Adjustment Programmes (SAPs) in the early 1980s<sup>36</sup>.

The Competition Act of Kenya (2010) provides among its objectives to "increase efficiency in the production, distribution and supply of goods and services" as well as the "promotion of innovation, the protection of consumers and enhancement of regional integration"<sup>37</sup>.

"Equity" is not listed as one of the goals to be pursued by competition institutions under the Competition Act of Kenya. This could well turn out to be a significant omission for a country with a long history of racial exclusion from economic opportunity (1895-1963) and a post-independence experience (1963-2015) of ethnic polarisation and conflict grounded primarily on issue of distribution of public resources, especially land (Kibwana: 1996).

## **Major Assumptions of Competition Theory: The Concept of 'Efficiency'**

Neo-classical economists argue that under conditions of perfect competition, there is both 'allocative efficiency' and 'productive efficiency'. Productive efficiency, as understood by neo-classical theorists of perfect competition, argues that goods and services will be produced at the lowest cost possible in a perfectly competitive market; and that this will result in a saving on the society's expenditure incurred in the process of production.

According to neo-classical economic theory, consumer welfare is maximised in conditions of perfect competition. According to this argument, nation-states should not interfere with the 'good of mankind' (Smith: 1776). Allocative efficiency means that in a perfectly competitive market, economic resources are allocated between the different goods and services produced in precisely the quantities which consumers wish. Secondly, it means that the wishes of consumers can be discovered from the price that consumers are prepared to pay on the market.

Neo-classical economic theory stands accused of making several "unworldly assumptions" about the nature and characteristics of markets<sup>38</sup>. Classical economics assumes that market mechanisms will operate in order to develop a rational international division of labour, which will optimise the world's productive resources (Swainson: 1980: 2).

What perfect competition means is that on any particular market there is a very large number of buyers and sellers, all producing identical (or homogeneous) products; consumers have perfect information about market conditions; resources can freely flow from one area of economic activity to another; and there are no impediments (or barriers to entry) which can prevent the emergence of new competition<sup>39</sup>.

Working from the basic presupposition of perfect competition, neo-classical economics derives its theory of general equilibrium which argues that all factors of production receive an income equal to their marginal product. General equilibrium theory argues that a producer will keep on producing and only stop at the point where the cost of producing a further unit (the marginal cost) exceeds the price he would obtain for it (the marginal revenue)<sup>40</sup>.

The trend towards concentration and centralisation of production, and monopoly profits, has brought to question the whole scheme of capitalist markets operating on the basis of competition between numerous firms producing identical products. Neo-classical economics does not address the problem of monopoly as a growing factor in the modern economy: on the contrary, it assumes there are many producers of homogenous products competing on the basis of price in the market at all times.

Baran and Sweezy demonstrated that by the year 1966, if there was any competition in the US economy it was between oligopolistic corporations<sup>41</sup>. However, the economic theory taught in US universities and business schools continued to stress that competition was the basic condition of the US market and of all markets in general.

Baran's other concern was that, by 1956, the unproductive sector of the US economy (represented by luxury consumers, unproductive 'industries' like advertising and finance, and government) had become 'well larger' than the productive sector<sup>42</sup>. This pointed to a 'crucial contradiction' of the economic system of the USA.

In Baran's view, the system's resources were not directed "in the line of welfare, abolition of exploitation, [and] freeing civilization from the wealth fetishisation" but towards the "progressive degradation of civilisation"<sup>43</sup>. For Baran, the defining marks of the monopoly-capitalist order are 'waste' and 'irrationality'<sup>44</sup>. For example, with respect to the automobile (motor-car) industry in the US, Baran and Sweezy argued that more than 25 percent of the purchase price in the period between 1950 and 1956 was accounted for by unnecessary model changes.<sup>45</sup>

Another weakness of neo-classical economics is that does not unravel the operations of the economy (in the sense that Adam Smith or Marx

understood the nature of their work) but is content with unjustified abstraction from real conditions in different countries in the world economy. In the 21st century, “economists are more liable to be recruited at higher levels from science and mathematics rather than from the classical social science disciplines”<sup>46</sup>. This situation is attributable to the deference accorded to “mathematics and statistics as opposed to more general knowledge of the economy and the method and critique of the social sciences” within the economics profession<sup>47</sup>.

Since perfect competition is usually unattainable and monopolies are a common feature in the real world, some writers have argued for a more run of the mill theory of ‘workable competition’. They submit that competition law that recognises these hard truths of the market ought to be based on four main objectives:

The first thing is that it will have to prevent agreements between individual firms which have the effect of restricting competition between them. Secondly, it will need to deal with attempts by monopolists or dominant firms to abuse their position and prevent new competition from emerging. Thirdly, it will need to ensure that workable competition is maintained in oligopolistic industries. Fourthly, it will need to monitor mergers between independent firms whose effect will be to concentrate the market and diminish the competitive pressures within it<sup>48</sup>.

Such a design for competition law recognises that price competition, which is usually presented as an inviolable condition of capitalism, no longer dominates capitalist markets<sup>49</sup>. Under conditions of monopoly, the monopolist is in a position to affect the market price of his products by reducing the volume of his own production.

A dominant firm may realise that if it earns large supra-competitive profits it will attract new competition and instead may settle for a quiet, uncompetitive life by selling at a depressed price which is sufficiently low to discourage other firms from entering the market<sup>50</sup>. Foster concludes that it is necessary for neo-classical economic theory to deny the reality of monopoly in order for the theory to preserve itself<sup>51</sup>.

## **Kenya and South Africa: The Case for a Comparative Examination**

Kenya and South Africa (RSA) share a broadly similar colonial history. Both Kenya and RSA were brought under British sovereignty in the late nineteenth century.<sup>52</sup> The State-sector was already well-established and was a major factor in the economy of Kenya and RSA at the end of white

minority rule in 1963 and 1994 respectively. RSA is usually seen as an exceptional case in Africa; while, further up north in East Africa, Kenya is seen as a regional exception.

Among the earliest settlers invited to Kenya to ‘open up’ the colony by Sir Charles Eliot, commissioner of the East African protectorate until 1904, were many South Africans. The settlers believed in the superiority of ‘European civilisation’ over the African way of life “... in some kind of vaguely conceived absolute sense, which was thought to have both moral and intellectual dimensions” (Leo: 34).

The settlers not only took their primacy for granted, but also seemed to lack any great concern for minimising the harmful effects of European settlement upon Africans. On the contrary, it was the effect of the African presence upon Europeans that was viewed with alarm (Leo: 35).

The 1902 Crown Lands Ordinance gave the commissioner power to sell or lease land to settlers. Sir Charles Eliot thought that Kenya would make a good white man’s country (Olivier: 1927: 63). The colonial government introduced in 1902 a hut tax whose chief purpose was to compel Africans to work on farms the government had allocated to British settlers (Leo: 34).

The 1918 Resident Labourers’ Act compelled the African ‘squatter’ to work for 180 days in a year for European landowners. By the mid-1920s more than half of all able bodied men in two of the largest ethnic communities in Kenya (the Kikuyu and Luo) were estimated to be working for Europeans (Leys; 1974: 31). Within the space of a generation they had effectively been converted from independent peasants, producing cash crops for the new markets, into peasants dependent on agricultural wage-labour (Leys: 31).

In 1960, Europeans controlled 7mn acres of land, which comprised about 50 percent of Kenya’s arable land and 20 percent of the country’s highly productive areas. In addition, 61,000 Europeans accounted for about 40 percent of the total wage bill in a country with 169,000 Asians and 7.8 million Africans (Ochieng’: 1992). In 1960, about 4,000 European farms accounted for 83 percent of the total agricultural exports of the country (Ochieng’: 176).

The negotiations held in Lancaster between 1960 and 1963 between the departing British administration and the incoming Africa regime of Kenya resulted in a constitutional bargain that would be mirrored thirty years later in the talks between the African National Congress (ANC) and the National Party in RSA. Kenya opted for the capitalist path at independence in a seminal economic policy document<sup>53</sup>.

The independence constitution of Kenya contained in Clause Six (6) a property rights clause that obliged the incoming African government to pay for settler farms. The compensation to settlers, as set out in the constitution, had to be paid in cash and not by bond: nationalist leaders, such as Oginga Odinga, the first vice-president of independent Kenya, viewed this as a drain on modest national resources (Odinga: 1967: 259).

The fundamental agreement of the negotiators in both cases was that disruptive changes to the economy at the end of white minority rule were to be avoided at all costs. The watch-words of the transition from colonial and apartheid rule to black majority rule in Kenya and RSA were: 'reconciliation' and 'stability'. Redistribution of wealth to the majority, a fundamental objective fuelling the liberation struggles in Kenya and RSA respectively, was subordinated to the objective to maintain 'stability' of the existing economic structures.

Thus the constitutional bargain to usher in the independence of Kenya in 1963 would serve as a template for the South African settlement to end apartheid between 1990 and 1994. The charge that the African elites that assumed power in Kenya in 1963 and in South Africa in 1994 accepted a 'sell-out' deal from the Europeans has spawned a political movement in South Africa that is committed to reverse the basis of that settlement.<sup>54</sup> The Mandela-Mbeki administration is accused of 'privileging the political struggle over the economic struggle' (Marais: 2001), resulting in a lop-sided settlement with De Klerk's Nationalist Party.

South Africa's Truth and Reconciliation Commission noted in its final report that 'violence' was the most 'consistent' feature in that country's history. Before the discovery of South Africa's wealth in gold and diamonds during the 1870s, Britain held only a few pockets of commercial and agricultural capitalism along South Africa's coastline. Those regions had been put under British sovereignty at the end of the Napoleonic wars in 1815.

The disintegration of the independent African peasantry in South Africa followed the establishment of a highly centralised mining industry in the country which needed a steady supply of cheap, unskilled labour.

The dismantled African peasantry would become the chief source of cheap labour, while a range of measures would be applied to guarantee and regulate the supply of labour. Administrative measures were introduced to establish and police a racial division of labour separating skilled European labour from unskilled African labour. The basis of British colonialism in South Africa during the final decades of the nineteenth century is summarised by Strachey in a revealing paragraph:

The question of who should use [African] labour and benefit from the surpluses which it produced, the British in mining or the Boers in farming, could, it turned out, only be decided by war [Anglo-Boer war (1899-1901)]. That this was in truth the issue is well commemorated by the terminology in use to this day [1959] in the City of London in regard to the matter. The City has always been, and still is, in the coining of its slang at least, delightfully frank.

How apt it is that South African gold-mining shares are known as 'Kaffirs'! Thus in a single word the underlying fact is revealed that what is really being exploited in South Africa is not only the gold of the Rand nor the diamonds of Kimberley, but the exceptionally cheap labour of the Africans, or Kaffirs, conveniently embodied in the mined gold or diamonds (Strachey: 1959: 92).

Some observers described apartheid as 'colonialism of a special type'<sup>55</sup>. Other writers saw in South Africa the development of a 'Two-Nation society' between the years 1900 and 1990. South Africa's 'Two-Nation society' was characterised by the phenomenon of the State subsidising the privilege of a 'racially defined minority [with] the trappings of a social welfare state' (Marais: 2001).

Lipton is a good representative of the 'liberal' viewpoint in South African historiography. Her survey of the growth of settler capitalism in South Africa reveals that Apartheid was a socially adaptive process. Lipton's account of the evolution of apartheid in South Africa from 1910 to 1970 is that although apartheid played a crucial role in shaping ... socio-economic patterns; its effect was not to make [RSA] a uniquely different society, but to shift the incidence of poverty onto blacks. This exacerbated many of the social evils and denied blacks the chance to escape from them which equality of opportunity, and various stages of the life-cycle, usually allows to at least some of the poor<sup>56</sup>.

This view assumed that capitalism was 'non-astrictive' or 'colour-blind': the industrial development of South Africa would lead, liberals argued, to the dismantlement of apartheid. The liberals argued that because apartheid could not be defeated politically, it had to be made unworkable economically until it collapsed. During the 1980s, apartheid was theorised as a peculiarly Afrikaner creation, since European countries had folded up their empires in Africa and Asia in the 1950s, 60s and 70s (Thompson: 1992).

The radical viewpoint in South African historiography, on the other hand, views apartheid as a complement to the capitalist system of South Africa from the inauguration of the Union of South Africa 1910 through Apartheid in 1948 up to the early 1990s. Representing the radical

standpoint, Ben Magubane saw apartheid “not as the result of a psychological aberration that one must deem irrational, but rather as a thoroughly rational arrangement supporting South Africa’s” white, hegemonic capitalism<sup>57</sup>.

Legum and Margaret pointed out that apartheid appeared to contradict a central argument of Marxist theory, which holds that those who control the key means of production, distribution and exchange would control the political machinery of their own society. In 1963, English-speaking South Africans controlled 99 percent of mining capital, 94 percent of industrial capital, 88 percent of finance capital and 75 percent of commercial capital<sup>58</sup>.

Despite this massive capital outlay in the hands of South Africans of British origin, the country was ruled by the Afrikaner section of ‘white South Africa’ between 1948 and 1990. The radicals’ response to this observation was that apartheid represented the ascendancy of white hegemonic capitalism in general, rather than a section of South Africa’s European community. In the radicals’ view, “apartheid was designed to secure labour for all capitals, not to deprive any employer of it” (Marais: 2001).

Amin summarises the debate around the relationship between capitalism and apartheid in a lucid paragraph:

South African capitalists developed ... a project aimed at moving up in the global system by means of an industrialisation process that would be firmly protected and supported by the state. The apartheid system was perfectly rational in that context. Cheap productive labour does not necessarily create a problem of reeling surplus value when the demand can be stimulated by raising the incomes of the ruling minority and by expanding some exports. The claim that there existed a fundamental conflict between apartheid and capitalism misunderstood what was at stake (Amin: 2001: viii).

Mamdani seems to occupy his own ground somewhere between liberal and radical historiography (Mamdani: 1996). Mamdani views apartheid as ‘late colonialism’, .i.e. basically a continuation of the British colonial policy of the 1920s. The 1922 Stallard Commission appointed by the British colonial administration in South Africa laid down the principle that an African should only be in the towns to “minister to the needs of the white man and should depart therefrom when he ceases to minister”. The ‘civilised labour policy’, introduced in 1924, reserved unskilled labour for Africans and placed African wages at about 10 percent of wages earned by whites (Olivier: 1927).



The ANC has been in existence since 1912. Between 1990 and 1994, the ANC claimed that upon assuming power it would establish a 'developmental State' and 'lead, co-ordinate and plan' an economic strategy aimed at: (i) job creation, and; (ii) redistributing resources to the poor. However, in the negotiations leading to the 1994 constitution, the ANC agreed to a clause in the constitution that would guarantee the Reserve Bank of RSA independence. The result of this accommodation by the ANC to the interests of capital was to effectively remove monetary policy from democratic oversight and accountability.

The ANC's economic policy during the Mandela presidency (1994-1999) and his successor Thabo Mbeki (1999-2008) was contained in two documents: the Reconstruction and Development Programme (RDP) and the Growth, Employment and Redistribution (GEAR). Despite their redistributive rhetoric, both the RDP and GEAR were compatible with three objects favoured by financial capital, i.e.: (i) privatisation; (ii) liberalisation and (iii) convertibility. The RDP advocated for strict limits on State spending, while GEAR went even further to view government spending as an impediment to economic growth.

GEAR prescribed fiscal austerity and aimed to reduce the public sector debt which stood at 56 percent of GDP in 1996 to 3 percent of GDP by the year 2000. GEAR strategy placed the duty of economic salvation on the private sector through private investment and privatisation. However, GEAR provided no detailed linkage between its macroeconomic linkages and industrial policy. The neo-corporatist vision to 'lead, co-ordinate and plan' a redistributive economic policy became frozen inside the ANC.

The RDP and GEAR policies showed a desire to distribute economic benefits widely across society without, however, raising the anxiety of capital-owners. The penetration of RSA financial markets by foreign capital was encouraged by the ANC, as was the migration of local capital overseas. The strategy of Black Economic Empowerment was introduced by the ANC and quickly became prominent in government tendering and procurement processes as well as in privatisation drives.

Marais argues that South Africa's economy is marked by three main features, two of which are endemic to most middle-income developing countries. Firstly, South Africa's economy is heavily reliant on commodity exports for foreign exchange. Secondly, South Africa's industrial sector appears to have been arrested in the semi-industrialised phase (Marais: 2001: 105).

The third feature and which could lend some credence to the claim of South African exceptionalism is that the country has well-developed transport, information and communications systems. Marais, however,

contends that South Africa's systems of communication and transport are 'inefficient', although those systems may be likened to those found in First World countries in terms of 'sophistication'.

Marais lists four conditions affecting South African industry that are also shared by a majority of African countries: low productivity, limited skills base, ageing plants, and a dependency on imports of capital goods. The general conclusion is that South Africa's integration into the world economy throughout the 20th century rested on three pillars: as a primary product (mainly minerals) exporter, an importer of capital goods and technology, and a net recipient of indirect portfolio investment and direct foreign investment by multinational corporations (Marais: 106). Marais is dismissive of the viewpoint that South Africa is an exception on the continent in terms of economic structure, calling it a "revisionist fantasy lacking supportive evidence" (Marais: 105).

Leys in his 1974 work on underdevelopment in Kenya argued that the country lacked an indigenous bourgeoisie that could catalyse industrial transformation (Leys: 1975). Leys' early work was located within the 'dependency tradition' and pictured the African elite that had ascended to power at independence as a 'comprador regime' that sought alliances with foreign capital, rather than devising ways to replace international capital on the local scene.

Leys' revised (1978) thesis was more ambivalent as to the soundness of the main arguments of dependency theory. Swainson, in her 1980 survey of multinational corporations operating in Kenya, was even more optimistic than Leys of the possibilities of Kenya launching itself along the path to industrialization (Swainson: 1980).

Swainson traced the development of an indigenous (i.e. African/black) capitalist class in Kenya to the colonial era. She argued that this class did not lack the capacity to usher in industrial transformation in Kenya, along the lines of the English bourgeoisie in the 19th century. Swainson located this class of African capitalists in the State sector.

According to Leo, Kenyan capitalism seemed such a success that by the mid-1980's even Marxist writers "did not take a non-capitalist development route seriously as an alternative for Kenya"<sup>59</sup>. By the early 1990s, however, matters had turned sour for Kenyan industrialisation. Coughlin argued that many forces conducive to rapid industrialisation in Kenya during the 1960s and 1970s sought to hinder it in the 1980s and 90s<sup>60</sup>.

He gave the example of multinationals and local industrialists who lobbied against tariff reforms that would help new industries to make intermediate inputs locally. Coughlin grouped together "merchants,

monopolists, and politicians” in Kenya who became ‘allies’ for the “quick kill” while also killing jobs and a whole range of industries that could have manufactured products like ‘screwdrivers, cutlery, pencils, ceramics and sisal bags (Coughlin: 1992)’.

Despite the shared historical ties and trajectories of colonialism and anti-colonialism, not many parallels have been drawn between the political economy of Kenya and RSA.<sup>61</sup> The colonial State in Kenya and RSA operated an economic system where the European settler minority enjoyed a monopoly in several departments including: (i) a monopoly over fertile land and the production of cash-crops like coffee and cotton; (ii) a monopoly in banking and marketing services; and (iii) job reservation where unskilled menial work was reserved for Africans.

Colonial marketing and processing facilities relied on the importation of capital-intensive technology managed by expatriates and controlled from abroad (Brett: 1974). Railway line branches were located in European farming areas. The colonial system of taxation discriminated against the African majority by levying hut and poll taxes on Africans exclusively.

Despite contributing the largest amount in the tax collected by the colonial administration, Africans received only modest investments in expenditure for health, education and housing. This is the general context within which competition policy and law must be anchored. A narrow focus on efficiency might not be in the best interests of African countries.

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## Endnotes

- 1 Birmigham: 1993; Boahen: 1985
- 2 Saad-Filho: 2003: 11
- 3 Ademujobi & Olukoshi: 2009: 4.
- 4 Ademujobi & Olukoshi: 4.
- 5 Gachuki & Coughlin: 1988: 91
- 6 Nyong'o: 2002: 22; Amin: 2014
- 7 Mehta: xxviii. See part III in this paper explaining 'productive efficiency' and 'allocative efficiency'.
- 8 The framing of these two questions is adapted from John Saul who poses the same questions in reference to the "labour aristocracy debate" in the African setting. For a summary of the 'labour aristocracy debate' in Africa see Foster: 2014; Zeleza: 1996.
- 9 According to Marx, "primitive accumulation" is that process which is not the result of industrial capitalist activity but its "pre-condition", Tucker: 1972. Rosa Luxembour, in contrast to Marx and some Marxist writers like Mandel, does not freeze "primitive accumulation" to the historical period (pre-1850) before the emergence modern industrial capitalism. Luxembour insists that modern industrial capitalism must engage in foreign conquests and imperialist wars (i.e., primitive accumulation) if the system itself is to continue to exist.
- 10 Berman & Lonsdale: 79
- 11 *Ibid*
- 12 Hollis: 2002: 235. See also Horn "[E]very approach to provide legal or non-legal protection of foreign investment has to deal with the problem of inequality of the parties involved, i.e. the sovereign host state on one hand, and, on the other, the foreign private investor, typically a foreign company or a domestic company controlled by foreign investors" 7
- 13 Braudel: 1976; Robinson: 1983; Buck-Morss: 2009
- 14 Robinson & Gallagher: 1953; Wright: 1976
- 15 The Robinson-Gallagher thesis is presented as a counter-narrative to the Marxist theory of imperialism (especially the version of Lenin: 1939), see Wright: 145.
- 16 Importantly, Strachey served in the British cabinet as the Minister for War during the Second World War.
- 17 Gutkind & Wallerstein: 1976: 182
- 18 Gutkind & Wallerstein: 182
- 19 Davidson: 1966: 202-3
- 20 Brett: 1974. It would appear that by the phrase "the negative effects so clearly visible in the present situation" Brett is referring to Africa's general condition of 'underdevelopment'.
- 21 ECA: 2013: 6; Rodney: 1972; Swainson: 1980; Leys: 1975; Nyong'o: 1992.
- 22 Abdalla Bujra and Samuel Lando 'Introduction' xiv.
- 23 Davidson: 1992: 197

- 24 Founou-Tchigoua: 2002: 155
- 25 Founou-Tchigoua: 155
- 26 *Ibid*
- 27 Tordoff: 2002: 14; Morten: 2011
- 28 Founou-Tchigoua: 155
- 29 Gray & McPherson: (2001):731
- 30 Coughlin & Ikiara: 1992
- 31 Fischer, Hernandez-Cata & Khan: 1998
- 32 221 US 1 (1911); Stelzer: (1986) 5
- 33 251 US 417 (1920); Stelzer: 10-19
- 34 This was the position of the European Court of Justice in *British Airways v Commission of the European Communities* (First Chamber Case T-219/99); Adeleke: 48.
- 35 Sutherland: 2000: 7.
- 36 The sort of “mixed-economy” preferred by Kenya’s founding President Jomo Kenyatta, and his cabinet minister in charge of economic affairs Tom J Mboya, was an economy that was “predominantly driven by the private sector, but with ample room for producer cooperatives, state-operated enterprises, and small holder production for the market” see Chege: 2007.
- 37 Section 3 of the Competition Act of Kenya 2010, compare with Section 8 (c) and (d) of the Competition Act of South Africa 1998.
- 38 Foster: 2014: 55
- 39 Whish:1985: 2
- 40 See Introduction: The theory of competition; Whish: 1985: 2
- 41 Baran & Sweezy: 1966
- 42 Foster: 2014: xvii
- 43 Foster: xviii
- 44 Foster: 40-1
- 45 Foster: 40
- 46 Milonakis & Fine: 2009: 15
- 47 Milonakis & Fine: 15
- 48 Whish “Introduction” 11
- 49 Foster: 2014: xiii
- 50 Whish ‘Introduction’ 7
- 51 See ‘Chapter 3 – Free Competition and Monopoly Capital’ Foster: 2014: 51-73.
- 52 Marais: 2001, dismisses the view that South Africa is an exception on the African continent. The argument for ‘Kenyan exceptionalism’ can be gleaned from Swainson: 1980. In contrast, Barkan: 1995 does not argue for a Kenyan exceptionalism. For a recent summary of the debate around ‘Kenyan exceptionalism’ and whose conclusion is that Kenya’s growth in the 1960s and ‘70s was closely paralleled on the continent see Morten: 2011: 2-23.

- 53 The full title of the 1965 publication by the government of Kenya is “African Socialism and its relation to planning in Kenya”.
- 54 The Economic Freedom Fighters (EFF), a political party that came third in the most recent elections in South Africa, and led by the erstwhile leaders of the ANC Youth League, has publicly expressed its aim to implement the Freedom Charter’s prescriptions on “nationalization of monopoly industries”, Bond: 2014; Odinga: 1967; New African.
- 55 The South African Communist Party (SACP) adopted the theory of “Colonialism of a Special type’ in a 1962 document called *The Road of South African Freedom: Programme of the South African Communist Party*.
- 56 Lipton: 1985: 18
- 57 Berger & Godsell: 1988: 287
- 58 Legum & Margaret: 1964: 108
- 59 Leo: 1984: 8. Leo considers that only a marginal group comprised of the “more ethereal [,] literary and philosophical Marxists” would probably go against the grain of “Marxists and non-Marxists [who] are as one in their acceptance of a capitalist development path for Kenya” 9.
- 60 See Coughlin & Ikiara: 1992.
- 61 Olivier: 1927; Leo: 1984; Leys: 1975; Okoth-Ogendo: 1991; Mandela: 1993. In his autobiography Nelson Mandela writes that he was inspired in his militancy during the 1950s and ‘60s by the ‘Mau Mau’ movement based in the central highlands of Kenya and the movement’s leader Dedan Kimathi.

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## 9

# The State Incentives to Oligopoly in Face of Small and Medium-sized Enterprises in Latin America

RODRIGO DE CAMARGO CAVALCANTI

*Doctor in Law by the Pontifícia Universidade Católica de São Paulo  
Brazil*

### **Abstract**

The participation of Micro, Small & Medium Enterprises (MSMEs) in the economies of the developing countries is essential, at the same time that we face a global increase of enterprises concentration in the sense of creation of large economic conglomerates that have the main world market shares.

The oligopolies' matter, especially in Latin America, is correlated to the democratisation and privatisation processes of the economy of those countries which occurred more intensely in the beginning of the 1990's, after the fall of the dictatorships and infusion of neoliberalism prevailing in the local State policies. Therefore, despite constitutionally most of the Latin-American countries are protected by rules that value the social justice and the distribution of wealth, the globalised economy, through economic liberalism, undertook a process that lead to the current scenario of oligopolistic presence of domestic or international enterprises, although normally with transnational size.

Henceforth, considering those conditions as paradigms of a structural condition conniving with oligopoly and consequently, the lack of incentive to the productive efficiency of MSMEs, there should be a discussion, especially within the Latin America scope, concerning the examples and

references associated to such issues and the possible solutions for implementation of conditions of development for those enterprises and, consequently, provide compulsion to the necessary increase of competition, for the sake of favouring the entire society.

## **Introduction**

According to the last study (2010) of the International Finance Corporation (IFC), a member of the World Bank, there are 125 million formal Micro, Small and Medium-Sized Enterprises (MSMEs) in the set of 132 analysed economies, including 89 million in emerging markets.

The participation of MSMEs in the economies of the developing countries is essential, at the same time that we face a global increase of enterprises concentration in the sense of creation of large economic conglomerates that have most of the world market share.

Those elements generate a challenge that will be emphasised herein, among others, which is the major existence of oligopolies in most of the national markets. Also in 2000, UNCTAD verified the oligopoly in those countries as a major issue to be tackled by governments and the World Bank working in partnership.

The oligopolies matter, especially in Latin America, is correlated to the democratisation and privatisation processes of the economy of those countries which occurred more intensely in the beginning of the 1990's, after the fall of the dictatorships and infusion of neoliberalism prevailing in the local State policies. Therefore, the globalised economy, through economic liberalism, undertook a process that lead to the current scenario of oligopolistic presence of domestic or international enterprises, although normally with transnational size.

In Brazil, as well as in several developing countries mainly in Latin America, three political programmes that created and still perform such condition, among others, are the following:

- the practice of the national champions theory, especially by contributions of public investment, thus building a private relation between the State and the large national enterprise, its stock in the stock exchange and the public interest for the profit;
- the indirect imposition of the government to the antitrust divisions of adopting a lenient posture against the acts of concentration so that certain economic and political agenda is met, despite the fact that in principle they give effect or strengthen the oligopoly, they

are encouraged by financing and investment in public programmes; and

- lack of parameters of the antitrust division to judge the acts of concentration associated to the legal and normative concepts of social justice and human dignity and preference to those of the merely economic theory of ‘social wellness’ (in excess of the producer/consumer).

Henceforth, considering those conditions as paradigms of a structural condition conniving with oligopoly there should be a discussion, concerning the examples and references associated to such issues and the possible solutions for implementation of conditions of development for those enterprises and, consequently, provide compulsion to the necessary increase of competition, for the sake of favoring the entire society.

The global oligopoly is nowadays the most characteristic form of supply while the centralisation of capital, combined with the decentralisation of production, commercial and financial management, reorganise the economy and geopolitics of the world. The mergers and ongoing acquisition on the planet since the end of the 20<sup>th</sup> century dramatically altered the international market power relationships, leading economies beforehand domestic to global performance in competitive levels which current boundaries are given by way of interdependence between companies.

In this sense, François Chesnais said that this oligopolistic condition refers to the interdependence between firms, including ‘firms not reacting to more impersonal forces coming from the market, but personally and directly to their rivals’.<sup>1</sup>

These take their mutual dependence marketplace, by all kinds of agreements (technical cooperation, joint determination of standards), of which not much fits the antitrust laws.

The constitutive relations of the oligopoly become in themselves, inherently, an important factor of barriers to entry, in which other elements (such as sunk costs or the magnitude of the investments in R&D) can then graft.<sup>2</sup>

In this scenario, since the 1980s, due to the economic crisis and the consequent adoption of neoliberal doctrine of the International Monetary Fund (IMF) and the World Bank, in force is a political and economic platform of deregulation of the financial sectors of developing countries, included therein Latin America, as well as a process of greater appreciation of the private sector to conduct themselves, of free competition and freedom of contract. The state, therefore, due to this booklet, should work towards minimum intervention in the market and the

internationalisation of the domestic economy as prerequisites for a good management of the economy.

With this policy, due to the inclusion of Latin American countries in a globalised international market, foreign direct investment rate (FDI) increased considerably. In Argentina, for example, while in 2000 the stock of FDI was about US\$21,140mn, in 2010 jumped to US\$29,840mn. In Brazil, in 2000 it was US\$51,946mn and in 2010 it went to US\$188,637mn. In Chile, in 2000 the amount was US\$11,154mn and reached the level of US\$60,146mn in 2010 – and then there was a considerable increase in all Latin American countries.<sup>3</sup>

This wave of internationalisation of Latin America economy has taken place since the 1990s, with the expansion of business in this region from various sectors of economic activity into new markets abroad.

### **Big Business and Oligopoly: Key Factors of Dissociation with a Defence Policy of SMEs**

Normally, the predominant perspective in studies on internationalisation focusses on companies in the internal factors that lead to this phenomenon.

In Latin America, there was a significant increase in FDI from the 1990s, a time when the economies of the region, from the neoliberal policies of the IMF and the World Bank, have adopted plans of monetary stabilisation and implemented market-oriented reforms (privatisation). More open to a growing oligopolistic competition, Latin American countries have seen some of its largest companies develop strategies to reach overseas markets as well as access to capital and technology.

However, we intend to draw attention to the effectiveness of the role played by the government to the success of multilatinas not only as deregulation agent of domestic economies but also in an attempt to foster by economic dynamism, including the promotion of expansion of certain companies. The trend of concentration of wealth and market in the hands of a few business leaders is one of the consequences of such policy, as the antitrust agencies cast a blind eye to major mergers and acquisitions (M&As) in the analysis of mergers.

Efficient international expansion of multilatinas depends much, simultaneously, of inorganic growth through acquisitions and joint ventures. Considering overseas acquisitions, compared to Latin companies of local operations, those of global reach make on average almost four times more joint venture operations and six times more business M&As.

What must be considered about the oligopoly capitalism in Latin America is that, 'in decreasing the base of accumulation that is relevant to capital, capital its own is responsible for destroying the excess of capital in operation. Companies break, obsolete or surplus production structures are eliminated, acts of the capital centralisation process, to keep running the capital in a smaller base of accumulation, with higher profits for those who remain'.<sup>4</sup>

Mexican and Brazilian economic conglomerates dominate the list of top investors abroad, followed by Chile and Argentina. Chile, in turn, has the largest number of companies on the list such as retailing and distribution of energy. Obviously, they are 'champions' in the concentration and centralisation of capital in their countries of origin in order to control much of varied economic activities.

On the emergence of national champions companies, says Leandro Bruno Santos, based on Michalet: "the multilatinas are those champions after a long historical process of concentration and centralisation of capital in their home bases under state support. The author relates the theory to a concrete situation, but it cannot be assumed that all multilatinas will be domestic champions, because it depends on historical and spatial conditions or otherwise, the particular conditions of each socio-spatial formation. The concentration and centralisation remain important as theoretical parameters, while the role of the state which had been raised should be analysed for its relevance in the broader process of capital accumulation and power."<sup>5</sup>

The specific concept of 'national champions' is considered by some scholars restricted in Latin America, Brazil, in the face of the policies of the National Bank for Economic and Social Development (BNDES). This Bank, a financial institution of the government, acts since 2002 practically performing loans to big companies in order to invest for the consolidation of those on the global stage. This purpose, namely, to encourage large domestic companies to become victorious competitors in the international market is the so-called 'theory of national champions.'

The economic policy of national champions is not restricted to direct, positive, monetary investment, but is part of a set of factors observed in much of Latin America, factors of which are the permission of certain concentration acts which would be in the government's aim.

What happens is the following: "we find a direct participation of the State not only to allow for the economic concentration, but also for its promotion. Such interference occurs always, in our view, for the sake of an irrational logic of preserving a biased structure of the concentration of

wealth in capitalism. We see therefore a reversal of nationalisation of enterprises: privatisation of the state in which it passes to undergo ever more intensely to gains and losses inherent in the market game.”<sup>6</sup>

There is, therefore, an indirect imposition of governments to antitrust agencies to adopt lenient stance in the face of mergers to fulfill certain political and economic agenda. Advocates, for example, Giovanni Dosi, an Economics Professor at the School of Advanced Studies Sant’Anna in Pisa, Italy: “I propose that developing countries build domestic oligopolies able to compete with foreign oligopolies, both nationally and internationally.”<sup>7</sup> For the supporters of this theory, there is no contradiction between competition policy advocacy and market concentration, especially if taken into account the global market.

The consequence is thus a “shared power without the need for overt collusion; the identity price is the general rule, and competition takes the form of physically indistinguishable differentiate products through design and particularly through advertising.”<sup>8</sup>

The national champions, therefore, ‘can benefit from loans guaranteed by the state or implicit support raising the rating of its debt and reduce borrowing costs. It also helps access to natural resources, specific budgetary allocations, tax benefits and exemptions by supervisory authorities.’<sup>9</sup>

In Argentina, for example, in 2007, in the cement market, the Antitrust Commission confirmed that three companies dominated 96 percent of the business. In short distance fixed telephony, Telefónica and Telecom controlled 80 percent of the market. After the engulfing of Quilmes by Ambev, 81 percent of the beer consumed in Argentina comes from a single Brazilian company. The Cablevision-Multicanal merger happened stating that, nationally, these two firms held ‘dominant’ position, with 51 percent of cable TV subscriptions.

Still, from 1999 to 2006, the *Comisión Nacional de Defensa de la Competencia*, Argentine antitrust agency, analysed 489 economic concentration, of which 94 percent were authorised, only five percent were subordinated to the fulfillment of any condition imposed by the agency and less one percent was denied.<sup>10</sup> i.e. low rates of impediment and even subordination to conditions in view of the amount of concentration led to the Argentine agency.

It is still worth considering that there is an obligation of analysis by the agency as they fall within the following thresholds (Law 25,156, article 8): acts involving the participation of companies or groups of companies in a quota equal or greater than 25 percent or more of the relevant market;



or when the sum of the total turnover in the country of all the companies concerned is more than the sum of US\$200mn; or even when the total turnover worldwide, of all the companies is more than US\$2,500mn, i.e. only large companies are subject to examination by the antitrust agency.

In Brazil, in turn, according to Law 12.529/11, the Conselho Administrativo de Defesa Econômica (CADE, the Brazilian antitrust agency) should analyse the merger that portray one of the following: at least one group involved in the operation has registered in the last balance sheet, gross annual sales or total turnover in the country, in the previous year to the operation, equivalent to or greater than R\$ 400,000,000.00 (four hundred million reais); and at least one other group involved in the operation has registered in the last balance sheet, gross annual sales or total turnover in the country, in the previous year to the operation, equivalent to or greater than R\$30,000,000.00 (thirty million reais) (Art. 88, I and II). As it turns out, it is also of great size and relevance of companies in the domestic market.

The oligopoly is also present vehemently in Brazil. In partnership with the British counterpart Edmund Amann, the expert in Brazil Werner Baer, Professor of the Department of Economics of the University of Illinois (US), investigated 19 sectors of the country and found a strong concentration in 14 of them, in which the top four companies hold over 60 percent of the market. The branch with less competition is the petrochemical, with a 91 percent rate; automotive industry (85 percent), wholesale trade (80 percent), mining (79 percent) and food and beverages (76 percent) respectively. The broadband internet in the country, in turn, in 2014, was controlled by just four companies: Hi, Telefonica, Net and GVT. They dominated 90 percent of broadband in the country.<sup>11</sup>

But even with very high levels of concentration in the Brazilian market, CADE, from January to July 2015, judged 192 cases of mergers, approving restrictions with 5 of them and not condemning any.<sup>12</sup>

In Chile, the Subsecretaría de Telecomunicaciones (telecommunications agency) reveals that in 2013, three companies of this sector concentrated 98.7 percent market share, with 37.34 percent Movistar, Entel 37.26 percent, and Claro 24.11 percent. The Chilean national air traffic, in turn, as reported by the National Board Aerea in 2010 was concentrated on LAN Express (40.8 percent) in the SKY Airline (16.9 percent) and LAN Airlines (38.7 percent). With regard to pharmacies, the newspaper Estrategia News informs that this sector is concentrated, in 2010, in three companies, namely: Salco (25 percent), Fasa (30 percent) and Green Cross (40 percent).

The *Tribunal de Defensa de la Libre Competencia* (TDLC), the Chilean antitrust agency, according to data from Organisation for Economic Co-operation and Development (OECD), from 2004 until March 2015 only 25 concentrations were submitted to that body, and that of the total, 11 mergers were approved, only two failed and in 12 cases the TDLC did not issue resolution about.

Chilean law does not provide numerical thresholds to define the scope of the inspection system. However, there is a Guide on concentrations which indicates that it will not be investigate those horizontal operations that are below certain Herfindahl–Hirschmann Index (HHI) levels. These thresholds are not standard closing because it does not exclude the possibility of control by the *Fiscalía Nacional Económica* (FNE) or the eventual notification of the operation to the FNE.

HHI thresholds included in the Guide to FNE on Concentrations are limited in scope, are not binding, and its application is dimensioned to horizontal operations submitted to the FNE, entity that reserves the right to investigate operations that do not meet the thresholds under one of the following special circumstances: (i) one of the parties involved is a potential competitor; (ii) a Party is a leading innovator and a strong independent competitor (a “maverick” company); or (iii) there are current or recent signs of coordination.

This oligopolistic situation presented in the Latin American country markets, as exemplified above in relation to three major economies that dominate the list of foreign investments, is strengthened by their governments, and shows a preference towards production efficiency at the expense of allocative efficiency and also limits the economic and political power already quite limited for SMEs.

The national market for Latin American countries in view of the low level of development, calls for a promotion by the government granting a greater contribution of SMEs, taking into account the requirements of those in the economy conditioned to the low levels of technology adoption, little qualification of its employees and/or the employer himself, a relative administrative fragility, and low productivity.

In this scenario, as indicated by Emilio Zevallos V., we come across with “the demands of the new economy that in the process of globalisation has developed a new production and institutional framework that calls for substantial improvements in business processes, flexibility, quality and low prices, and, for countries, systemic productive development policies.”<sup>13</sup>

On the other hand, given the current globalised environment, Ana Maria Nusdeo ponders that, in practice, the possibilities are remote that

countries like Brazil issue differing decisions of those countries where the headquarters of multinational companies are based. However, Nusdeo points out that there must be a careful and an effort “affirmation of competition to protect the interests of the country, with the imposition of remedies deemed necessary to do so, or the even more radical solution of denial of operation.”<sup>14</sup>

The high degree of productive efficiency of big corporations, combined with the ease in raising credit and also to the indulgence of the state and, more than that, to a state policy model encouraging these major economic actors, reduces the possibility of SMEs in the trading market in the face of consumers, making it difficult to insert new actors into the economy, new actors that can contribute to the development of countries in which institutional and financial fragility, with social consequences, is latent.

Research conducted by Santander Bank in 2013 showed that 99 percent of companies in Latin America are micro, small and medium enterprises. The study, conducted with data’s from the World Bank, the International Labour Organisation, the Inter-American Development Bank and the Economic Commission for Latin America and the Caribbean showed that about half of these companies are in the informal sector and that a high percentage of them respond to a goal of self-employment or livelihood, not an ambitious or growth potential, as well as informality and access to credit are compromised.<sup>15</sup>

It is also worth to note the study of Krekel, Van Der Woerd and Wouterse, for whom there are three categories of small and medium enterprises whose extinction is a natural consequence of the antitrust current policies in the face of high levels of concentration. One type concerns those companies ‘whose direction, production methods and financial or commercial structure are inappropriate; they are working at the limit of profitability and only remain for border protection force, still in force, or by a more or less precarious persistence’<sup>16</sup> linked to the past. They have become so marginal companies whose ‘natural selection’ of the market does not give truce.

Another type of SMEs endangered situation with regard to family businesses that still resist the demand of professional managers, and belonging to a single owner, or a single family without extinction of this continuing process. And lastly, we can mention those that are far from achieving an optimal size, and “its products can be industrialised, for lower costs, by important companies.”<sup>17</sup> These small and medium enterprises as well, according to the aforementioned authors, succumb to the concentration of larger companies.

## Conclusion

With this analysis, it is understandable that the development of small businesses, therefore, regarding antitrust policies, basically depends on the following programmes:

- effective control *ex ante*, on the debasement of oligopolies through stricter decisions with respect to the concentration acts (worth pointing out that all those under the supervision of the antitrust agencies are, as a rule, large acts);
- clearer and more objective insertion of human rights in the analysis of the antitrust agencies, teleologically to the dignity of the human person in order to ensure proportional balancing to the concentration acts effects on the widest possible number of factors; and
- finally, the encouragement of SMEs by sharing information of companies forming part of the oligopolistic group with other companies in the sector, under the supervision of the antitrust agency (in order to avoid undue and untied information exchanges for the decision goals), with the aim of minimising the technological and informational imbalance involving distribution logistics methods and storage products, among others, to a larger structural and performative balance, always with proportionality and reasonableness (in order to avoid exacerbated transfer efficiencies).

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## 10

# Promoting Innovation to Foster Competition, Economic Development and Growth in Developing Economies

VIVEK GHOSAL

*Richard and Mary Inman Professor and Director of Graduate Studies, School of  
Economics Georgia Institute of Technology, Atlanta, USA; Research Fellow, CESifo,  
Munich, Germany; and Visiting Professor, European Business School  
Wiesbaden, Germany*

### **Abstract**

This paper provides an overview of selected national policies, institutions and types of organisations that can help foster innovation in developing economies. It discusses some of the essentials that are needed to organically stimulate innovation in products and services within a country. Stimulating a meaningful amount of innovation within a country is essential for developing more mature and relatively competitive markets that, in the longer run, will promote economic development and growth, and sustained development of human capital. The paper provides a brief illustration of innovation and value chain in global coffee markets.

### **Introduction**

The literature on innovation encompasses a wide range of issues related to patents on products and processes, copyrights, trademarks, among others, and enforcement of intellectual property rights (IPRs). This paper discusses selected issues related to innovation, the key benefits it bestows

on national economies, manner in which innovation can promote competition, and the government policies and initiatives that can foster innovation in developing economies. The objective is not to provide a comprehensive overview, but to highlight some key issues that may help decision-making in framing policy.

More specifically, the paper addresses some issues related to institutions, organisations and policies that are likely to organically stimulate innovation in products and services, and technological development within a country. In the longer run, these processes will also facilitate the development and growth of internal markets, along with making them more competitive. The policy insights from this paper will be helpful in achieving higher economic growth and employment, and foster sustained innovation and industrialisation in developing economies. These aspects are also key to reducing the disparities in economic opportunities.

The paper briefly examines some issues in the relationship between innovation and competition; and various institutions and organisations that foster innovation and development of technologies. It discusses selected issues related to regulatory and competition policies, and their links to innovation and provides a brief illustration of innovation in products and services in the global coffee markets. It concludes with some policy prescriptions.

## **Innovation and Competition**

Innovation is viewed as critical to fostering the growth of markets, generating new products and processes, generating efficiencies and improving economic welfare. The relationship between innovation and competition is bi-directional and complex: the degree of competition among firms has been recognised as one of the important factors influencing innovation; and, greater innovation is viewed as one of the factors that may affect competition and growth of markets.

The relationship between innovation and competition is, therefore, important for several reasons. If innovation generates growth of markets and increases efficiency, then creating institutions and markets that foster innovation are vital to increasing economic welfare. Further, if relatively more competitive markets generate greater innovation, then antitrust and regulatory policies, for example, would need to be structured and enforced appropriately to facilitate competition.

As has been recognised in the literature, instances where patents create monopoly rights (e.g., in pharmaceuticals) can prove to be complicated in assessing economic welfare effects as we need to trade-off the potential



increase in market power with the availability of new innovative products. However, even in an industry like pharmaceuticals, if there exist multiple well-resourced incumbent firms – or potential entrants – who can generate inter-patent competition, then these competitors can offer disciplining effects on prices. An important role played by competition law and enforcement would be to monitor markets effectively to, for example, minimise mergers and acquisitions (M&As) that might lead to very high levels of market concentration.

In the economics literature, the bookends linking innovation and competition are the contributions by Schumpeter (1934, 1942) and Arrow (1962). Schumpeter predicted that larger firms with rent earning opportunities will generate greater innovation. Arrow, in contrast, predicted that atomistic firms in competitive markets will generate greater innovation. Recent important theoretical contributions by Aghion et al. (2005) predict a non-linear relationship between innovation and competition, with *intermediate* levels of competition delivering the highest levels of innovation. The writings by Aghion and Griffith (2008), Cohen and Levin (1989), Ahn (2002), and Gilbert (2006), for example, provide excellent reviews of the broader theoretical and empirical literatures.<sup>1</sup>

One way to view how more innovative and entrepreneurial economies and markets can foster more competition is as follows. The literature generally shows that countries that generate greater overall innovation are also those with high rates of new firm startup and entrepreneurial activity. While not all of this startup and entrepreneurial activity will be successful, some will succeed and grow to be larger firms.<sup>2</sup>

It is this process of creative destruction that generates new and innovative firms and products that over time may replace the incumbents and constrain their market power. These new entrepreneurs and firms can provide effective competition to the incumbents creating a more competitive environment.<sup>3</sup>

## **Institutions and Organisations that Foster Innovation**

Significant initiatives, policies and institutions are needed to stimulate innovation in developing economies. Without this, domestic innovation will suffer, retarding growth and development in the longer run.

Examining the literature, there appears to be no single defining item that helps foster innovation and technological development within a country. The ingredients appear to include clear rules and protection of IPRs, accommodative economic policies to support entrepreneurship and innovation, an overall economic environment and regulations that support

business creation and development, availability of private and public financing, and a variety of key organisations.

### **Intellectual Property Rights (IPRs)**

There needs to be a well-defined system of protection of IPRs, accompanied by clear infringement protections.<sup>4</sup>

Perhaps the most important point to note for developing countries is that the presence of a well-run and enforced IPR regime is almost essential for organic growth of innovation within the country. A lot of this discussion gets clouded by comparisons between the more developed and less developed countries. But this is missing an important point. Unless each country develops a realistic and meaningful IPR system within the confines of their own country, within-country innovators have less incentives to innovate. Local entrepreneurs and innovators need IPR protection as this provides them the incentives to innovate.

Lack of organic growth of internally developed technologies and innovation will likely to result in lower rates of growth and economic development in the longer run. While the optimal IPR protection period can be debated and varies across countries, developing economies need a well-structured IPR infringement system to protect innovators and entrepreneurs, and stimulate growth.<sup>5</sup>

### **Business Incubators and Accelerators**

Incubators and accelerators have played an important role in development of nascent firms, products and technologies.<sup>6</sup> While most of the well-known and successful incubators and accelerators, but certainly not all, appear to be concentrated in the relatively more developed countries, there are important lessons for developing economies. The objectives of incubators and accelerators, broadly speaking, are to foster innovation, entrepreneurship and creation of new businesses.

An *incubator* is an organisation designed to increase the likelihood of success of entrepreneurial firms. Incubators bring in external management team to manage an idea, and can focus on tasks such as job creation, professional services, training, networking, venture capital financing, and utilisation of specific technologies.<sup>7</sup> There are several different types of incubators. The university-based incubators (UBIs) and university-associated business incubators (UABI) primarily aim to connect entrepreneurial talent and skills to specific types of technologies and services. The private business incubators, in contrast, provide any aspect of a wide range of support and services. The international business

incubators, in contrast to all of the above, concentrate on international firms that want to access foreign markets and resources.<sup>8</sup>

The emergence of *accelerators* followed the growth and maturation of the incubator model.<sup>9</sup> An accelerator can be either an advanced stage incubator which assists more mature entrepreneurial firms, or they can be an organisation that contains hybrid business incubation programmes designed for incubators to enter the market. Some of the characteristics of accelerators include competitive applications process, pre-seed investments, and limited-duration and intensive mentoring.<sup>10</sup>

**Table 10.1** briefly summarises some of the key similarities and differences between incubators and accelerators.<sup>11</sup>

<b>Table 10.1: Some Comparisons between Incubators and Accelerators</b>		
	<b>Incubators</b>	<b>Accelerators</b>
<b>Duration</b>	1 to 5 years	3 months
<b>Business Model</b>	Rent; non-profit	Investment, can also be non profit
<b>Selection</b>	Non-competitive	Competitive, cyclical
<b>Venture Stage</b>	Early, or late	Early
<b>Mentorship</b>	Minimal, tactical	Intense, by self and others
<b>Venture location</b>	On site	On site

Historically, in the development of incubators and accelerators, the US attained significant benefits and growth. It has been noted that one of the important barriers for the development of incubators in Europe was the lack of entrepreneurship and the under-development of seed financing. It has also been noted that many incubators, particularly in Europe, did not screen potential firms on a balanced set of factors, but concentrated on the characteristics of the firms' market or the management team. It has been observed that firms' survival rate is positively related to a more balanced screening profile.<sup>12</sup>

**Table 10.2** presents selected examples of accelerators, the amounts of funding, and some of the success stories in terms of the startup firms.

<b>Table 10.2: Selected Examples of Accelerators</b>			
<b>Name (Start Year)</b>	<b>Country (Location)</b>	<b>\$Total (\$Average)</b>	<b>#Startups (Selected examples of startups)</b>
Y Combinator (2005)	USA (Silicon Valley)	\$4,030 (5.8)	694 (Dropbox, AirBnb, Strip, Optimizely, Zenefits)
TechStars Boulder (2007)	USA (Boulder)	\$250 (3.2)	77 (DigitalOcean, Gearbox, SendGrid, FullContact)
AngelPad (2010)	USA (San Francisco)	\$232 (2.7)	85 (Critticism, Postmates, MoPub, ElasticBox)
TechStars Boston (2009)	USA (Boston)	\$200 (2.4)	83 (Localytics, Kinvey, EverTrue, GrabCAD)
Seedcamp (2007)	UK (London)	\$131 (1.1)	118 (Transferwise, Basekit, GrabCad, Profitero)
DreamIT Ventures (2008)	USA (Philadelphia)	\$124 (1.9)	63 (SeatGeek, SCVNGR, Adapt.ly, MindSnacks)
Mucker Lab (2012)	USA (Santa Monica)	\$111 (5.8)	19 (Surf Air, Retention Science, Lifecrowd, Younity)
RockHealth (2010)	USA (San Francisco)	\$72 (1.5)	49 (Omada Health, Kit Check, CellScope, Sano Intelligence)
Flashpoint (2011)	USA (Atlanta, Geo)	\$64 (1.7)	38 (Ionic Security, Pindrop Security, Springbot, Lucena)
LaunchpadLA (2009)	USA (Los Angeles)	\$62 (2.4)	26 (Tradesy, Chromatik, ChowNow, Preact)
Springboard (2009)	UK (London)	\$54 (2.2)	25 (PagerDuty, Hassle.com, Birdback, PlayMob)
Portland Incubator (2009)	USA (Portland)	\$52 (2.4)	22 (VendScreen, Cloudability, Orchestrate, Vadio)
StartmateLink (2011)	Australia (Sydney)	\$17 (0.8)	21 (Scriptrock, Ninja Blocks, Bugcrowd, Bugherd)
FounderFuelLink (2011)	Canada (Montreal)	\$12 (0.3)	37 (oomf, Notesolution, Seevibes, Playerize, Urbita)
Chinaccelerator Link (2010)	China (Shanghai)	\$11 (0.3)	31 (OrderWithMe, Aylien, Splitforce, Piktochart)
Le CampingLink (2011)	France (Paris)	\$10 (0.2)	48 (Sketchfab, infinit, docTrackr, Augment, qunb)
Rockstart Accelerator Link (2011)	Netherlands (Amsterdam)	\$10 (0.2)	39 (3Dhubs, Wercker, Syndicate Plus, PastBook)
* \$Total (\$Average) refers to the total (average) funding made available (\$ millions).			

Incubators and accelerators are multifaceted organisational forms to meet specific needs. They can be private, public, or public-private partnership (PPP). For developing economies, there is a potentially important role of government in later two, but also important to facilitate and incentivise private participation.

There is meaningful evidence that relying on public investments and initiatives only to stimulate innovation and entrepreneurial activity may often lead to limited success. International evidence points to private being more successful overall. Some of the underlying reasons relate to less administrative, oversight and project content inefficiencies. Some of these lessons in comparative analysis of incubator and accelerator successes and failures are important for developing economies.

#### **University Based Collaborations and Science Parks**

There is increasing evidence that university-based science parks can foster innovation and entrepreneurship. Studies show that university-based technology ventures can lead to significant knowledge flows from universities to incubator firms, and affect the likelihood of survival of startups. Studies also find that the for-profit university technology transfer offices are positively related to new venture formation, and that the more traditional university and non-profit transfer offices are more likely to correlate with the presence of university-based business incubators.<sup>13</sup>

Studies also find that a high-technology firm's propensity to make effective use of the university parks' resources and support increases with the lifecycle stage of the company.<sup>14</sup> Finally, some studies find that the number of spin-out companies created are positively associated with rules on intellectual property protection, royalty regime of the university, and the business development capabilities of the university technology transfer offices.<sup>15</sup>

**Table 10.3** presents a few university-based incubators. It reveals the wide variation in the types and number of institutions that form such organisations. The information on the institutions involved are mostly from the website of UBI Index (<http://ubiindex.com>).

**Table 10.3: Selected Examples of University-Based Incubators**

Name (Type, Start Year)	Country (Location)	Institution(s)
SETsquared (UBI, 2003)	UK (Bristol, Southampton, Bath, Guildford, Exeter)	University of Bath, Bristol, Exeter, Southampton, Surrey
ATP Innovations (UBI, 2000)	Australia (Sydney)	University of Sydney; University of Technology, Sydney; Australian National University; University of New South Wales
IncubaUC (UBI, 2002)	Chile (Santiago)	Pontifical Catholic University of Chile
Industry Accelerator and Patent Strategy (UBI, 2013)	Taiwan (Hsinchu City)	National Chiao Tung University
Instituto Genesis PUC-Rio (UBI, 1997)	Brazil (Rio de Janeiro)	Pontifical Catholic University of Rio de Janeiro
TEC Edmonton (UBI, 2004)	Canada (Edmonton)	University of Alberta
DTU Symbion Innovation (UBI, 2009)	Denmark (Copenhagen)	Technical University of Denmark
Melbourne Accelerator Program (UBI, 2012)	Australia (Melbourne)	University of Melbourne
HUST Science Park Development Corp. (UBI, 2001)	China (Wuhan)	Huazhong University of Science and Technology
NDRC (UBI, 2008)	Ireland (Dublin)	Dublin City University; Dún Laoghaire Institute of Art, Design and Technology; National College of Art and Design; Trinity College Dublin; University College Dublin
Chrysalis (UBI, 2012)	Chile (Valparaíso)	Pontifical Catholic University of Valparaíso
National Chiao Tung University Business Incubation Center (UBI, 1998)	Taiwan (Hsinchu City)	National Chiao Tung University
iMinds (UBI, 2004)	Belgium (Ghent)	University of Antwerp; University of Leuven; Ghent University; Vrije Universiteit Brussel
TechColumbus (UABI, 2005)	USA (Columbus)	Ohio State University; Columbus State Community College; Otterbein University; Denison University
Montpellier Agglomeration Business & Innovation Centre (UABI, 1991)	France (Paris)	Montpellier University
Hub China (UABI, 2013)	China (Beijing)	Capital Normal University; Beijing Technology and Business University; North China University of Technology
Los Angeles Cleantech Incubator (UABI, 2011)	USA (Los Angeles)	University of Southern California; University of California, Los Angeles; California Institute of Technology; California State University, Northridge
Stiftelsen Chalmers Innovation (UABI, 1999)	Sweden (Gothenburg)	Chalmers University of Technology
Nanotechnology Incubator (UABI, 2005)	Mexico (Monterrey)	Instituto de Innovación y Transferencia de Tecnología de Nuevo León
Nuvolab (UABI, 2011)	Italy (Milan)	Università Cattolica del Sacro Cuore; Scuola Superiore Sant'anna

It has been noted that science parks can be an important strategy in the overall strategy or development of technologies and fostering innovation. One study using Italian data, for example, reveals that the science parks attracted skilled entrepreneurs, that incubator-related firms had better success rates related to technology adoption and technology-related collaboration with universities, and easier access to business capital including public subsidies.<sup>16</sup>

Other findings in this literature include a positive relationship between incubators and economic growth (Abetti, 2004). Further, evidence appears to find that by acting as open innovation intermediaries, publicly supported incubators were able to transfer knowledge from large firms to society (Clausen and Rasmussen, 2011), and that incubator and venture capital support influenced technology commercialisation and the performance of new ventures (Chen, 2009).

Universities can generate enormous knowledge and innovations. This needs to be harnessed via university-based science parks and incubators in the overall strategy of organic development of technologies and fostering innovation. Incentivising researchers and faculty in STEM (Science, Technology, Engineering and Mathematics) areas to participate in innovation and entrepreneurial processes will facilitate local generation of innovation and entrepreneurship in developing economies.<sup>17</sup>

The information and learning from the alternative models and experiences across countries can be useful in framing of policies to encourage formation of such organisations in developing economies.

### **Other Policies**

There are other standard instruments that governments have used worldwide for stimulating innovation. These include, for example, government subsidies and research funding. R&D subsidies, for example, is a common instrument used in many countries. The second instrument – direct research funding – has much larger variation across countries. These can be targeted to specific industries that governments may feel important for future growth and development. Areas could include critical sectors such as pharmaceuticals and generic medications, telecommunications technologies, alternative energy technologies, among others.

While government subsidies for research are a relatively common instrument, the use and size of this instrument varies considerably across countries. Developing economies in particular may be prone to allocating far less resources to this area. While this at times is justified given the

pressing needs in other areas such as alleviation of poverty, it is important to recognise the longer run benefits that may accrue these resources.

## **Role of Regulatory and Competition Policies**

The institutional and organisational characteristics are designed to stimulate innovation and technological development. In thinking about the innovation-competition nexus, some regulatory and policy dimensions are explored.

While the precise relationship between innovation and competition is debatable, there is ample evidence that economies that generate greater innovation are more successful in the longer run. When evidence on innovation is examined, it is clear that it does not come from any one group of firms or product category. Important innovations are generated by the smallest as well as the largest firms in the economy.

Further, innovation came arise in high-technology areas like ICT, pharmaceuticals and biotechnology, as well as in a wide range of other areas like processed food products and beverages, agriculture, transportation, among others. In addition, evidence shows that smaller firms generate innovation in a more cost-effective manner than larger firms; for example, evidence from many markets shows that the R&D cost per patent is often lower for smaller firms.

First, we consider the lifecycle aspects of firms, growing from small startups to larger corporations. In coffee markets Lavazza, a prominent Italian and global coffee company originally started within in a small grocery store in Turin, Italy. Starbucks started in 1971 opening its first small store in Seattle's Pike Place Market. Some of the most influential technology companies that have at various points in time redefined markets and consumers' lives, the names that come to mind include Nokia, Alibaba, Apple, Microsoft, Amazon, among others.

Perhaps the most interesting aspect of these companies is that all of them started as 'tiny' startups, and many of the most influential technology companies literally started in peoples' garages. The reason these companies were successful are very complex. But many of the institutional and organisational issues have generally been influential in ensuring higher likelihood of startups maturing to well-established and stable businesses; this is true in a wide ranging set of economies in Europe, North America, and some Asian countries. This implies that the economic and regulatory policy environments need to be structured in a manner to facilitate the creation and growth of new companies.



Second, the regulatory policies, institutions and enforcement need to clearly facilitate more open internal markets and competition. There are ‘sector’ regulators – typically, for example, in energy, transportation, banking and telecommunications – who are tasked with maintaining the vibrancy of markets in their specific areas. While they play an important role, they are not sufficient by themselves due to issues related to political intervention and regulatory capture. This implies an important role for (ideally) independent competition law enforcement agencies to provide an added layer of checks and balances.

Third, we need a well-structured competition law and enforcement environment. This will be complementary to the overall economic and regulatory policies. With respect to competition law enforcement, there is perhaps a fundamental conflict between small vs. large firms in an economy. As small, entrepreneurs and firms want relatively easy entry, access to capital, among other aspects, to succeed. As large, firms want entry to be difficult and costly, in order to preserve their economic rents.

Think of a nascent telecommunications or internet or online content provider. They would want easy access to network (net neutrality), capital, among other aspects to enter and grow. A large telecom or internet or online content provider, on the other hand, would want almost exactly the opposite. This implies that to get buy-in of all types of businesses into a common competition laws and enforcement mindset is a challenging task.

Examining consumers’ preferences, they would prefer markets that are innovative and provide them with greater choices regarding the range of products, quality, and low prices. While large firms provide many of these attributes, in important part the delivery of these attributes and vibrancy of markets depends on the ease of entry, entrepreneurship and competition.

Further, there is an important issue regarding stability of businesses. Historical evidence from developed and developing economies shows that small businesses, on average, have much higher failure rates. Larger businesses, on average, are more likely to provide greater stability to the markets.

The relative balance between small and large businesses is, therefore, rather nuanced. While smaller business provide much needed vibrancy to the markets, larger businesses may bring greater stability, substantial R&D and innovation footprint, among other aspects. The above discussion implies that an ideal market structure for optimal longer-run delivery of growth (e.g., incomes, investment, and employment), competition,

innovation, among other attributes would be one where relatively smaller and larger firms coexist.

It is a challenging task to address the potential importance and behaviour of smaller vs. larger businesses towards competition initiatives, and broader buy-in of initiatives that will foster competition in markets. Competition law and its enforcement, therefore, have to ensure that markets remain relatively competitive and facilitate the emergence and growth of new businesses, and foster innovation.<sup>18</sup>

## **Coffee Markets: An Illustrative Example and Scope for Innovation**

Innovation encompasses a wide range of issues related to patents on products and processes, copyrights, trademarks, among others, and enforcement of IPRs. Before moving to summarise a set of policy prescriptions, the paper provides a brief example from coffee markets to illustrate the multifaceted aspects of innovation, and what developing countries may need to do to move up the value chain.<sup>19</sup>

Coffee is one of the top commodities globally, and coffee beans are produced by many countries. The top coffee bean producing countries in 2014 were (in descending order):<sup>20</sup> Brazil, Vietnam, Columbia, Indonesia, Ethiopia, India, Honduras, Mexico, Uganda and Guatemala. However, the value-chain for coffee is rather complex. The broader processing steps related to roasting, grinding, blending and flavoring are very important and add substantial value.<sup>21</sup>

Sophisticated and prominent multinationals like Nestle (including Nespresso), Starbucks, Costa Coffee, Lavazza, among others, have devoted significant resources related to R&D (*e.g.*, in processes related to the mix of roasting, blending and flavoring), branding (trademarks) and marketing to elevate their standing in global markets, earn profits, and employing thousands of workers. While these companies are multinationals now, a prominent Italian coffee company Lavazza originally started within in a small grocery store in Turin (Italy), Starbucks started with its first small store in Seattle's Pike Place Market, and Costa coffee started in London with a small operation of selling coffee to few caterers and their first coffee shop would not be established till a few years later.<sup>22</sup> All of these firms had tiny beginnings. Their rise to multinational status occurred via innovation in products and services, branding and trademarks.

To simply produce a commodity like coffee beans and sell a basic ground coffee product is typically not sufficient to rise up the value chain.

Why is rising up the value chain important? Higher profit margins. And higher profits allow for potentially greater investments to be made to grow the businesses beyond local and national markets. In turn, this expansion would result in increased employment, incomes for the workers, and other opportunities. Without the requisite broader investments in R&D and innovation, branding (trademarks) and marketing, it is very difficult to elevate the business to a higher, multinational level. To rise in the value chain and reap greater profits, one of the root inputs is innovation in products and services.

## **Policies to Foster Innovation, Entrepreneurship and Growth**

Innovation and related policies need to be thought of in full spectrum which includes patents, copyrights and trademarks as well as the adequate enforcement of intellectual property rights. As noted earlier, more innovative and entrepreneurial economies and markets can foster greater competition, economic growth and development via the process of creative destruction. This dynamic generates new entrepreneurs and firms that can provide effective competition to the incumbents creating a more competitive environment. This dynamic also helps markets grow and create opportunities for investment and employment.

The core innovation issues related to protection of intellectual property and its enforcement are distinct from the regulatory and competition related policies. Innovation related policies therefore should be thought of as standalone, and not commingled with other policies. The latter approach may lead to a diffused focus and not produce best results in the longer run.

Cumulatively, the above issues point to the difficult balancing act policy-makers have to undertake to ensure the competitive and innovative vitality of markets in promoting growth and stability of smaller businesses, as well as not discouraging growth of businesses from small to medium to large. The challenge for governments, therefore, is to ensure that the conditions are ripe for emergence of new entrepreneurs, and entry and survival of small businesses, as well as ensure participation of larger businesses in the nation's growth.

Below is the discussion on a *two-tiered* strategy that governments in developing economies can follow to boost innovation.

**A. Tier-one**

A well-structured IPRs' regime and infringement protection includes patents, copyrights, trademarks, and related issues. This will ensure that entrepreneurs and innovators within the country have their creative ideas and innovations protected. In the longer run, this provides incentives for more individuals and businesses to innovate. As noted in the paper, lack of such a regime will thwart domestic innovation and entrepreneurship in the longer run.

**B. Tier-two**

This constitutes what could be thought of as a suite of complimentary policies that will foster innovation in the economy.

Governments can create National Science and Technology Foundations. These can be designed to provide support in the areas of resources, funding, technical advice, and operational guidance for high quality research projects. Such funding can be targeted to specific areas of national need and comparative advantage.

There are complementary vehicles via which governments can promote innovation. These include encouraging University-based research and entrepreneurship, which have been successful in numerous countries. In addition, governments can set up innovation incubators and accelerators on their own, in cooperation with universities, as well as in PPPs. Incubators and accelerators, in different forms, can provide critical support to entrepreneurs and small business to generate funding, management of innovative ideas, patenting, successful commercialisation of innovation, among other aspects.

While current research reveals that these types of organisations can be effective in boosting innovation, evidence shows that private, as opposed to public institutions, deliver better results. Perhaps an optimal strategy in this dimension is to foster creative PPPs to stimulate innovation and entrepreneurship.

To create more fluid and open markets, governments can examine where their country stands in the World Bank's 'Doing Business' reports.<sup>23</sup> For example, the indicators point to costs and time involved in opening a business. The indicators also point to regulatory and policy burdens to start new businesses. Governments can systematically examine these items and reduce the burdens on creation and growth of businesses. These will greatly facilitate emergence of a vibrant entrepreneurial culture and create new and innovative businesses.

Both regulatory and competition laws and enforcement must incorporate innovation (as well as production and service efficiency,

broadly speaking) as a focus of the policy objectives. These will likely bring benefits related to greater longer-run innovation, increased entrepreneurship, generation and success of smaller businesses, and their role in imposing competitive discipline to markets and the larger firms.

There are traditional forms of support such as offering R&D subsidies and small business financing specifically targeted to innovative activities. While these can greatly help generate innovation and growth, they typically tend to be limited by governments' resource constraints. Policymaking can be targeted to specific areas of national need and comparative advantage.

Overall, the sets of policies noted above need to be framed and implemented synergistically and with a longer-run view.

## Endnotes

- 1 Ghosal and Ni (2015) provide a brief overview of this literature. For more detailed expositions, see OECD (2006) and OECD (2009)
- 2 It is instructive to note that virtually all of the new economy giants at this point – like Uber, Microsoft, Apple, Alibaba, Google, among many others – were very small startups at one point. While these are the successful example, thousands of others did not succeed
- 3 As an example, in pharmaceuticals and biotechnology markets we observe meaningful inter-patent competition within numerous defined therapeutic classes and this serves to offer competition to incumbents and those who may have patented earlier
- 4 *E.g.*, Scotchmer (2004a, 2004b) and Stiglitz (2008) provide extensive background materials and views on these topics. Also see Hassan et al. (2010) for issues related to developing countries.
- 5 For discussion of some of the IPR and innovation related issues in developing economies, see, for example, Chen and Puttitanun (2005) and Hassan et al. (2010). Stiglitz (2008) provides a discussion of broader issues related to IPR and patents, but also a wider set of policies and investments that governments need to make to stimulate innovation and growth. Chen and Dahlman (2004), Dahlman and Utz (2007) and Dahlman et al. (2008) provide deeper insights into broad-based knowledge and innovation issues in developing economies.
- 6 See Ghosal (2015) for a concise overview.
- 7 The Batavia Industrial Center (New York, 1959) was the first US incubator, but the broader growth of this type of organisation did not occur until the 1980s. Aerts et al. (2007) provides details on how incubators guide firms to increase likelihood of success, and promote innovation and entrepreneurship
- 8 *E.g.*, Lewis et al. (2011)
- 9 *Ibid*
- 10 Miller and Bound (2011) note that accelerators have largely been a private-investor driven phenomenon.
- 11 Wu (2012), Miller and Bound (2011) and Cohen (2013) provide a more elaborate discussion of similarities and differences.
- 12 *E.g.*, Aernoudt (2004) and Aerts et al. (2007).
- 13 *E.g.*, Rothaermel and Thursby (2005a, 2005b) and Markman et al. (2005).
- 14 *E.g.*, McAdam and McAdam (2008).
- 15 *E.g.*, Lockett and Wright (2005).
- 16 *E.g.*, Colombo and Delmastro (2002).
- 17 For example, Chen and Dahlman (2004), Dahman and Utz (2007) and Dahlman et al. (2008) discuss alternative mechanisms including education and training that can be synergised to increase knowledge growth and innovation. These insights can be combined with the learning from the accelerator and incubator literatures to provide a comprehensive strategy for stimulating innovation
- 18 Baker (2007) and Golodner (2001), for example, spell out the links between competition policies and innovation and growth of markets.

- 19 This example was motivated by the discussants' comments to provide example of scope for innovation and growth in specific markets in developing countries. The example I provide is for coffee as it is widely grown, and is consistently in the top-5 commodities globally.
- 20 <http://www.worldatlas.com/articles/top-10-coffee-producing-countries-2014.html>
- 21 See, for example, the links below for a broad perspective on coffee markets and the value chain:  
[http://ww2.unime.it/ema/index.php?option=com\\_content&view=article&id=57&Itemid=45&lang=en](http://ww2.unime.it/ema/index.php?option=com_content&view=article&id=57&Itemid=45&lang=en)  
[http://www.investopedia.com/articles/investing/103114/starbucks-example-value-chain-model.asp?header\\_alt=b](http://www.investopedia.com/articles/investing/103114/starbucks-example-value-chain-model.asp?header_alt=b)  
<http://acetforafrica.org/wp-content/uploads/2014/08/Coffee-Dalberg.pdf>
- 22 For brief histories of some of the companies see:  
Starbucks: <http://www.coffee.org/History-of-Starbucks>  
Lavazza: <https://en.wikipedia.org/wiki/Lavazza>  
Costa: <http://www.costacoffee.ae/costa-coffee/the-costa-way/history/>
- 23 <http://www.doingbusiness.org/>

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Section III:

# Competition Reforms as a Tool for Public Welfare

Integrating elements of competition reforms into  
sectoral and for overall economic reforms to enable  
developing country consumers and producers derive  
measurable benefits



# Government Regulations and Private Sector Development in the Grain Market Operations of India

SURAJIT DEB

*Associate Professor in Economics  
Aryabhatta College, University of Delhi  
India*

## Abstract

Governments in developing countries often control the private sector in grain market operations to restrict the market power or speculative trading that seems to go against the food security objectives. However, the controls and interventions have not only held back the growth of marketing and distribution networks for the farm produce, but also prevented developing a competitive private sector in the Indian agricultural sector. This paper evaluates the reform initiatives undertaken by the government and points out the direction of future measures for a larger private sector involvement in the grain sector.

## Introduction

The food grain market in India operates with major government involvements on marketing, public procurement, distribution and buffer stock operations. Generally speaking, these controls and interventions are based on the conditions of production shortfalls and scarcities with the conviction that free trade would not maintain the domestic grain price stability. However, the controls on marketing-movement-storage meant for pursuing the government procurement-distribution-stockholding

operations virtually allocates any space for the free-market and competition to play a role.

The government in recent years has come out with several policy documents and many of them, viz., Expenditure Reforms Commission's Report on Food Subsidy,<sup>1</sup> Excess Food Stocks, PDS and Procurement Policy,<sup>2</sup> Long Term Food Grain Policy,<sup>3</sup> Report of Committee of State Ministers of Agricultural Marketing to Promote Reforms,<sup>4</sup> Restructuring the Food Corporation of India,<sup>5</sup> etc., recommends for a larger private participation in the country's grain business.

Moreover, policy measures such as the National Policy on Handling, Storage, and Transport of Food Grains, 2000; Removal of Control on Food Grains, 2002; Agricultural Marketing Reforms, 2002, Removal of Prohibition on Agricultural Commodities under Forward Contract (Regulation) Act, 2003, can be seen as steps to remove these restrictive provisions and promote competitive structure in grain marketing and trading. Several other provisions, viz., direct-marketing, pledge-financing and negotiability of warehouse receipt system are also likely to facilitate participation of private firms in the domestic and global grain trading. But, while the process of reforms is yet to be completed, governments (both at the Centre and state) have often continued to use such restrictive provisions on private trading to counter supply shocks and price fluctuations in India.

While the legislative/administrative controls and regulations diminish the incentives structure of the private traders and corporations, the interventionist instruments, viz., high support price, buffer stock operations, open market sales, export ban, stock declaration order etc. create the remaining roadblocks for the agribusiness in the country.

This paper evaluates the scope for private sector participation in India's grain (rice and wheat) economy. It provides a brief account of the government's interventionist instruments and measures of control. An account of Food Corporation of India's (FCI) cost of grain handling operations is included. The paper provides a description of various policy recommendations relevant for private participation in the grain sector. In order to examine the nature of competitive elements, market powers within the rice and wheat (flour milling products, biscuits, bread and breakfast cereals) industries is analysed. The feasibility and areas of private participation in grain business is deliberated and summary/policy implications are provided.

## Instruments of Government Control

The Department of Food and Public Distribution (DOPD) within the Ministry of Consumer Affairs, Food and Public Distribution, the Commission for Agricultural Costs and Price (CACP) of the Ministry of Agriculture and the FCI provides the institutional structure for grain management in India. The Ministry makes the grain policy for implementation, the CACP advises on price policy, while the FCI undertakes the procurement, handling, transport, storage and distribution of grains on behalf of the government.

Further, the Directorate of Marketing and Inspection (DMI) of the Ministry of Agriculture exercise its control on marketing and trading of the grain produce in India. The functions of DOPD in the grain sector are: i) implementation of the public distribution system (PDS) with special focus on the poor, ii) provision of storage facilities for the maintenance of central food grain reserves and promotion of scientific storage, iii) formulation of national policies relating to export, import and buffer stocking, iv) quality control and specifications of food grains, and iv) administration of food subsidies relating to rice, wheat and coarse grains. The instruments of government interventions and control are briefly discussed:

**Minimum Support Price and Procurement:** The government announces the minimum support prices (MSP) for procurement on the basis of the recommendation of the CACP before the harvestings in *rabi* or *kharif* crop season. The food grains procurement policy bears the twin objectives of ensuring MSP to farmers and also ensuring availability of food grains to the weaker sections at affordable prices. The FCI and various state agencies establish a large number of purchase centres at *mandis* to procure wheat, paddy and coarse grains under the price support scheme and rice under the statutory levy scheme. The extensive MSP operation of FCI over the years has resulted in sustaining the incentive structure for the rice and wheat growers.

However, since a major portion of the public procurement originates from a few surplus states, it is argued that the support prices cater only to the surplus states. The government also procures rice through the *levy system*, which is a compulsory procurement mechanism through which a part of the produce is bought from the farmers, traders or millers at a price lower than the market.

**Issue Price:** The Central government issues wheat and rice to various state governments at central issue price for the purpose of carrying out PDS. It is believed that the off-take from fair price shops (FPS) is determined by the difference between ration and market prices. On the other hand, the stock allocation for rationing and the quantum of ration off-take have been found to bear an impact on the market price of food grains.

**Buffer Stocks:** The buffer stocks are required to carry out PDS and welfare schemes, ensure food security during the production shortfalls, and stabilise prices during periods of price fluctuations. As on April 01, 2015, the central pool food grain stock remained at 170.84 lakh tonnes of rice, 172.21 lakh tonnes of wheat and 100.39 lakh tonnes of un-milled paddy. The stock level with FCI bears a destabilising influence on the open market grain prices. Technical groups under the chairmanship of Union Food Secretary recommend the buffer stocking norms for different quarters, which is given in Table 11.1.

Table 11.1: Food Grain Stocking Norm for the Central Pool (Revised on January 22, 2015), Lakh MT				
	Operational Stock		Strategic Reserve	
	Rice	Wheat	Rice	Wheat
1 <sup>st</sup> April	115.80	45.60	20.00	30.00
1 <sup>st</sup> July	115.40	245.80	20.00	30.00
1 <sup>st</sup> October	82.50	175.20	20.00	30.00
1 <sup>st</sup> January	56.10	108.00	20.00	30.00
Source: <a href="http://www.fci.gov.in/stocks">www.fci.gov.in/stocks</a>				

**Open Market Sale Scheme (Domestic):** The open market sale scheme (domestic) of food grains has been based on various models as per the guidelines given by the Ministry. Although, price stabilisation during lean months is kept as the main objective of this scheme, yet surplus stocks are often disposed on account of limited storage capacity or to reduce the carrying costs. Initially, there was a directive that the FCI sale may be confined to Roller Flour Mills, *Atta Chakkies*, Super Bazaars and Cooperative Stores, but the OMSS (D) in recent years has been carried out for retail sale, bulk sales, sale to small processors, sale to small private traders and sale to bulk consumers.

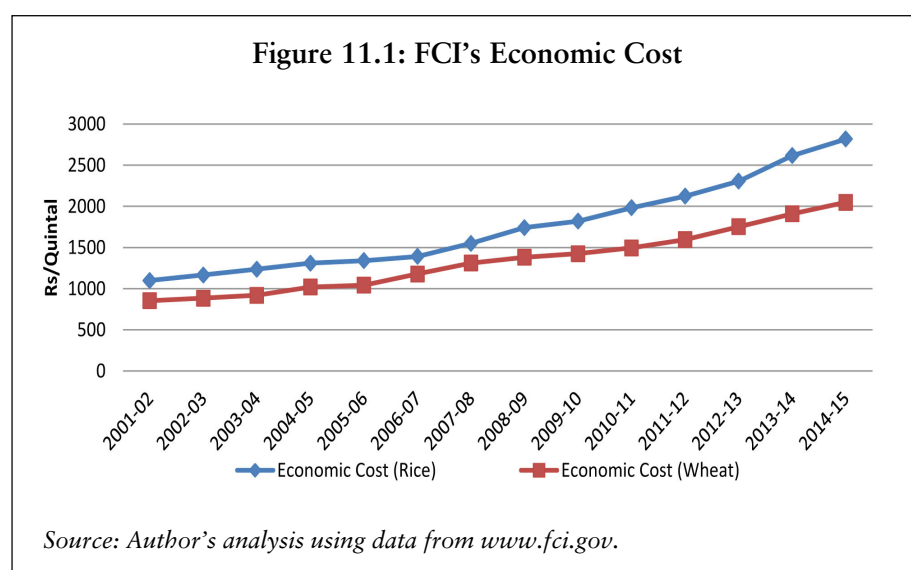


## Cost of Public Grain Handling Operations

The FCI operation is viewed as a major grain market intervention and has attracted the policy analyst's attention due to its high cost and corresponding budgetary subsidies. It is important to note that government policies bear a substantial impact on FCI's business. For instance, every MSP revision results in higher costs of grains and stock maintenance above buffer norms add to its carrying cost.

The counter-critics therefore claim that subsidies may not be an appropriate pointer to FCI's uneconomic operations, since it arises due to the multiple objectives of providing price support to the producer and consumer subsidy to the poor as well as preventing the nation's food insecurity. However, the FCI enjoys autonomy in its field operations, viz. procurement decisions, negotiation for RBI credit, storage decisions, grain movement plans and the choice of transport. It seems that while government policies may remain responsible for the high FCI costs, a part of the cost can apparently be attributed to the inefficiency in FCI operations.

The previous research have found that FCI in India remained a high cost and bureaucratic organisation, which needed reorganisation in order to fulfill its functions more cost-effectively.<sup>6</sup> Several explanations were offered in the literature to explain as to why the private trading cost is lower than FCI cost of operations. It is claimed that private traders carry out direct purchase from farmers by avoiding the *mandi* charges, reuse gunny bags several times unlike FCI, transfer grains by trucks which are



cost-effective and have lower transit losses. As a result, participation of competitive firms in the grain market operations often feature in the government agenda for inflicting efficiency in the system and also make budgetary saving on FCI subsidies.

Figure 11.1 provides information on the recent increases in FCI's economic cost of rice and wheat. The critics have also pointed out that much of the food subsidy actually covers the costs of FCI's inefficiency and therefore demand that FCI trim its grain market operations.

### **Reform Initiatives to Promote Private Business:**

It is argued that given the sensitivity of the agricultural sector in terms of food security, many governments have been hesitant to leave this sector to unregulated market forces.<sup>7</sup> But, the removal of legislative controls and administrative orders as well as the introduction of agricultural marketing reforms can initiate competitive grain businesses in many developing countries. The competitiveness element can be taken to mean a larger involvement of private firms in the marketing-storage-movement operation of grains.

It is relevant to note that the involvement of private sector or its collaboration with the public sector in a public-private-partnership (PPP) model for the production and distribution of public goods and services have been successfully implemented in several countries. Thus, provision of goods and services in the areas of education, health, poverty programs, urban infrastructures and housing, public utilities (drinking water, electricity, sanitation, waste management, etc.), social services and even government administration have witnessed private participation at the global level. It may be mentioned that the notion of private participation is rejected at times due to the apprehensions of poor service quality and reduced governmental responsibility. The various arguments for and against private participation of goods and services can be distinguished as in Table 11.2.

In the recent past, several government reports and commissioned studies in India have recommended to reform the grain market operations by mainly removing the restrictive provisions, injecting efficiency into FCI operations and liberalising the grain marketing. It can be discerned that the government foresees the FCI's role to change from the major buyer and subsequently re-establish the private sectors in the areas of procurement, storage and distribution of food grains in India (Table 11.3).

Table 11.2: Arguments for and against Allowing Private Participation	
Arguments for	Arguments against
Savings on Public Finance	Administration and Service Monitoring Costs
Efficient Provider with Quality Service	Profit Motive Costing Service Quality
Increase Efficiency and Innovation	Price Collusion Resulting in Higher Price
Increases Accountability	Reduces Public Accountability for Service Failure

**Agricultural Marketing Reforms:** Although the production of agricultural commodities in India is free from controls, the same is not true for their marketing and processing that remains under state control. The whole geographical area in the state is declared a *market area* falling under the jurisdiction of *market committees*. Since, any sale or purchase outside the market yard is prohibited by the act; there is a virtual monopoly of government regulated markets in most of the states.

Further, there are controls on processor to buy only from the notified markets, incidence of multiple taxes on the processing activities and restrictions on storage and movements. All these have worked as deterrents for the development of competitive marketing systems in the country, and have also failed to provide the incentive structure to the farmers, traders and industries. The Expert Committee on Agricultural Marketing suggested various legislative reforms and reorientation of policies, such as, promotion of direct marketing, organized retailing etc. Subsequently, the Inter-Ministerial Task Force on Agricultural Marketing Reforms identified several priority areas to restructure agricultural marketing, and prepared the *Model Act on Agricultural Marketing* to enable the states frame their own Agricultural Produce Marketing Development and Regulation (APMDR) Act.

<b>Table 11.3: Policy Recommendations for Reforms in Grain Markets</b>	
<b>Study/Policy Reports</b>	<b>Major Recommendations</b>
Expenditure Reforms Commission's Report on Food Subsidy, GoI [2000]	<ul style="list-style-type: none"> <li>• Greater involvement of the state government and private sector in the procurement and storage operations</li> <li>• Rationalise the tax/levy structure on procurement from different states</li> </ul>
Cost of Acquisition & Distribution of Food grains by FCI, ASCI [2001] commissioned by Ministry of Consumer Affairs, Food and Public Distribution	<ul style="list-style-type: none"> <li>• Restructure FCI</li> <li>• Federalise FCI among states</li> </ul>
Working Group on PDS and Food Security for the 10 <sup>th</sup> Plan, GoI [2001]	<ul style="list-style-type: none"> <li>• Decentralised PDSMSP in line with cost of cultivation</li> <li>• Review Essential Commodities &amp; APMC Act</li> </ul>
Excess Food Stocks, PDS and Procurement Policy, Virmani and Rajeev [2001]	<ul style="list-style-type: none"> <li>• State government and private sector's participation in procurement and storage</li> <li>• Decentralised PDS</li> </ul>
Long Term Grain Policy GoI [2002]	<ul style="list-style-type: none"> <li>• Universal PDS, MSP in line with cost of cultivation</li> <li>• Improve FCI's performance</li> <li>• Larger private participation</li> </ul>
Report on Central Government Subsidies in India, GoI [2004]	<ul style="list-style-type: none"> <li>• Reduction of MSP</li> <li>• Replace the present 2-tier system of APL-BPL issue price with food-coupons for BPL</li> </ul>
Final Report of Committee of State Ministers, in charge of Agricultural Marketing to Promote Reforms, GoI [2013]	<ul style="list-style-type: none"> <li>• Amend APMC acts</li> <li>• Substitute licencing system of traders/commission agents</li> <li>• Remove physical barriers to trade like check gates,</li> <li>• Single window registration for traders- Levy market fee only for the first transaction</li> <li>• Differentiate between genuine service provider and hoarders under Essential Commodities Act</li> <li>• Specify provisions for private wholesale markets and terminal markets</li> </ul>
Report of the High Level Committee on Reorienting the Role and Restructuring of Food Corporation of India, GoI [2015]	<ul style="list-style-type: none"> <li>• Revisit its MSP policy</li> <li>• Relook at NFSA commitments</li> <li>• Hand over FCI's procurement operations to specific states</li> <li>• Private sector to compete with state agencies in grain procurement</li> <li>• Outsource FCI's stock operations, Initiate negotiable warehouse receipt system</li> </ul>

**National Policy on Grain Handling, Storage & Transportation, 2000:** This policy recommends better grain storage practices, viz., automation in handling and sliding of stocks, and also minimise on the transportation costs. It further proposed that the bulk grain handling facility be built with private participation on the basis of Built-Own-Operate (BOO) model.

**Futures and Forward Contract in Agriculture:** It is often argued that future trading can provide two major advantages to product marketing, viz., price-discovery and efficient price-risk management. In India, the removal of prohibition on future trading was notified for some agricultural items and their trading was organised through recognised exchanges, subject to rules and regulatory procedures prescribed by the Forward Market Commission (FMC). Future trading in agriculture involves various regulatory authorities, viz., FMC, Reserve Bank of India (RBI) and Securities and Exchange Board of India (SEBI). Apart from these three regulatory authorities, other four commodity exchanges were authorised. The agricultural commodities that were given permission for trading are soya oil, guar seed, guar gum, chana, jute, rubber, pepper, turmeric, wheat, *kapas* (cotton) etc.

**Negotiable Warehouse Receipt System:** The market believes that cash-settled contracts are liable to generate speculative trade, thus physical deliveries are essential to provide the equilibrating mechanism in future demand and present supplies. The warehouse facility, quality certification system and transferability and negotiability of warehouse receipts backed by legal provisions remain crucial for the growth of agricultural futures markets in the country. The system of negotiable warehouse receipts could potentially eliminate various transaction costs involved in the grain marketing and also reduce the cost of maintaining public infrastructures.

The Expert Committee had suggested universalising the system of warehouse receipts in future trading so as to raise volumes and minimising the transaction cost. Since the quality aspect bears a crucial risk element in agricultural future trading, its success depends on to what extent the quality risk is covered in the contracts. The declaration of reform in this direction can be viewed as a step towards removing restrictive provisions and liberalising grain marketing in the country.

## Concentration of Market Power

Spiraling price increases or price volatility in the presence of market power and speculative trading in grains markets have often been identified as major risks to food security in developing countries. Mckeen [2015] has recently illustrated how the corporate global food chains or the financial and structural power of corporations can set the food security rules to their advantage. The governments often justify control measures for the private sector on the grounds of containing the speculation and safeguarding the interest of farmers and consumers. The market power refers to the ability of a firm to raise and maintain price above the level that would prevail under competition. A firm with market power bears the ability to engage in unilateral anticompetitive behaviours, viz., affect either the total quantity or the prevailing prices in the market.

The Herfindahl index (also known as Herfindahl–Hirschman Index) remains as the standard measure to evaluate the size of firms in relation to industry, viz., the market concentration. The measure is defined as the sum of the squares of market shares of the firms within the industry, where the market shares are expressed as fractions. The index value ranges from 0 to 1, depending on the presence of large number of firms to a

**Table 11.4: Herfindahl Index of Concentration for Rice and Wheat Based Industries (2001-2010)**

Years	Rice	Flour Milling Products	Biscuits	Bread	Breakfast Cereals
2000-01	0.06	0.00	0.14	0.22	0.55
2001-02	0.07	0.00	0.14	0.30	0.56
2002-03	0.07	0.00	0.16	0.25	0.51
2003-04	0.09	0.00	0.19	0.25	0.48
2004-05	0.10	0.00	0.22	0.24	0.34
2005-06	0.06	0.00	0.25	0.16	0.35
2006-07	0.09	0.01	0.24	0.24	0.35
2007-08	0.09	0.02	0.24	0.26	0.37
2008-09	0.09	0.02	0.25	0.34	0.44
2009-10	0.11	0.02	0.23	0.36	0.47

*Note: The numbers of sample companies are above 30 for both Rice and Flour Milling Products, above 16 for Biscuits and above 5 and 4 for Bread and Breakfast Cereals, respectively.*

*Source: 'Market Size and Shares' (various issues), Centre for Monitoring the Indian Economy.\**

single monopoly producer. Since the index takes into account the relative size distribution of firms in a market, its value approaches to zero when a market is occupied by a large number of equal sized firms and reaches to one, when the market is controlled by a single firm.

The Herfindahl Indices of Concentration is analysed to examine the market power in the rice and wheat based industries (Table 11.4). The evidence of market power is much lesser in rice and flour milling products, but somewhat higher in the processed segment that uses wheat and/or rice, viz., biscuits, bread and breakfast cereals. The near zero values of the indices indicate perfect competition in the flour milling industry. Since no individual participant in the market bears significant market power, anticompetitive behaviours, e.g., price setting, use of predatory pricing, creating barriers to entry for potential new competitors, etc., do not appear likely to take place.

## Feasibility and Areas of Private Sector Development

Success of a reforms programme depends not only on the combination of policies but also on their timing and sequencing. The grain market reforms agenda should ensure that the decontrol and deregulation measures are initiated for the beginning of private participation. However, the reformist policies should not remain limited to removing the marketing and movement restrictions, but also address fundamental issues like the MSP and the buffer stock policies.

The MSP of almost all agricultural produce in the past have ruled above the market price and at times the world price. Rising MSPs provide the biggest roadblocks for the private participation because it finds procurement at economically unreasonable MSP genuinely problematic. Similarly, the scale of FCI procurement also poses greater uncertainties for the private traders and corporations involvement at times.

While the Central government may start the set of reformist policies, the task of implementation remains with the state governments, since agriculture remains under *state subject* in India. It may be mentioned that in the recent past the effort level of states has remained low in fully adopting the Model APMC Act. In the same way, there remain uncertainties with regard to government resolution banning the movement restrictions under the Essential Commodities Act (ECA). The permission to carry out purchase, movement and trade is yet to be fully granted by the modifications of ECA and APMC Acts. It therefore appears that the marketing reforms and decontrol on movement restrictions could provide the vital incentive for generating the private response. Subsequently, the

modernisation of grain storage and supply chains would become necessary to provide the impetus to private participation.

A reduction in the size of public procurement could lead to more produce reaching the market and there is an obvious scope that the post-harvest activities (cleaning, drying, storage and transport) associated with grain handling to pick up. The participation of firms in grain business would get a further boost when the sector gets the permission to establish and operate agricultural marketing infrastructures and supporting services. The private sector can also be involved to carry out the procurement operations on behalf of the FCI and fulfil the government's PDS responsibilities. The private sector's involvement in the grain business can be expected to move further in the direction of processing and exports once the restrictive policies are removed.

There remain certain gaps and contradictions within the existing provisions and policies that intend to reform the grain business. For instance, future contracts necessitate that prices are determined by market forces without any government control, and no single buyer-seller-regulator bear any undue importance on prices. But, the present MSP policy eliminates the price risk through assured government procurement mechanism. Thus, when prices are fixed by the MSP policy and do not adjust except through change in government policies, there remains a little incentive for hedging a risk.

Likewise, the policy of promoting a processor-grower arrangement cannot be successful without the judicial support of contract enforcement and a crop insurance mechanism. Finally, the requirement of capital can be expected to grow with the grain market liberalisation in India. The private participation would expand if an appropriate mechanism for providing advances against stocks is provided. The negotiable warehouse receipt system can provide the source of inventory credit in the financial transaction of agricultural commodities. One can expect a higher private involvement with the creation of a legal framework for the negotiability and transferability of warehouse receipts.

## **Summary and Policy Implications**

The government controls and regulations impose some obvious costs on the private grain business in India. At the same time, the public management undertaken within regulated market condition is found to be costly so that it already created huge subsidy burdens on the government. It is being recognised that the public grain handling operations are intertwined around such complex control and regulatory instruments



that their executions at times remain beyond the capacity of the Central and/or state governments.

It therefore appears that the dependence on control and regulatory mechanism has to be reduced for carrying out the grain market operations, and there is a strong case for substituting these as much as possible by the market mechanism. Similarly, the ECA restricts the movement of agricultural produce across states boundaries and also imposes stock limitations on the traders. In the same way, the Agricultural Produce Marketing acts necessitates that traders buy produce only from regulated markets. These acts and restrictions have only made the accomplishment of direct contractual relationship between the grower and processor difficult.

A larger private participation, which bears a built-in competitive mechanism, can be expected to improve the incentive structures of the grower, trader and end-consumer. The entry of private sector may inflict competition in the grain procurement process and make farmers get better returns from the FCI, which acts as a monopsony buyer. The improvement in agent's incentives structures could make the grain market activities more market determined. This may lead to enhancement in the market-size with more produce reaching the market instead of getting used for the public stock maintenance. A set of reform measures that allow private participation can facilitate the use of modern technologies and exploit the potentials of a whole range of value chains in the grain sector.

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## Endnotes

- 1 GoI 2000
- 2 Virmani and Rajeev 2001
- 3 GoI 2002
- 4 GoI 2013
- 5 GoI 2015
- 6 BICP 1990, World Bank 1999, Gulati, Kahkoken and Sharma 2000, ASCI 2001, GoI 2002 and Chand 2003
- 7 Schwager 2015

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# 12

## Role of Government in Promoting Sustainable Economic Growth through Competition Reforms *Exploring the Challenges in the Competition Regime in Tanzanian Case*

FREDERICO RINGO

*Director, Fair Competition Commission  
Dar es Salaam, Tanzania*

DEO JOHN NANGELA

*Director, Restrictive Trade Practices, Fair Competition Commission  
Dar es Salaam, Tanzania*

### **Abstract**

Competition enhances the levels of productivity through efficiency gains, widens the frontiers of market access through increased entry opportunities that in turn, results into increased investments and continuous innovation to capture new market niches. This paper illustrates the role of the Tanzanian government in competition reforms. While it supports the view that achieving sustainable economic growth in most developing countries is a function of regulatory reforms; it argues that such reforms must essentially aim at eliminating or minimising costs of doing business in order to stimulate investments, industrialisation, and ultimately providing new employment opportunities that adds to stability and total socio-economic and political welfare. Given the available opportunities in Tanzania, strong political commitment in promoting regulatory reforms is required for Tanzania to leap frog from a low to middle income before 2050. This paper also argues that successes or

failures of competition reform, or any regulatory reform, depend on the political will of the government of the day.

Taking Tanzania as our case study, this paper will analyze the government's role in the competition reform process in this country, and the role which competition policy has been playing in the economy in promoting healthy markets, consumer welfare, employment, innovation and industrialisation.

Finally, in order to realise the highest returns from competition or any other regulatory reforms, participation of key competition stakeholders is vital. The paper will examine the synergies that exist or need to be established between those who support the competition reform agenda and those who are beneficiaries of the reforms.

## Introduction

Tanzania, a country that had erstwhile pursued a state-planned economy, is now one of the developing countries that adhere to the tenets of liberalised economy policies. Its adherence to such neoliberal philosophy is not without reasons or history. As from 1961 when it attained its independence to 1966 the country's socio-economic life had a capitalist flavour. The private sector was taking the lead in contributing to growth.

However, in 1967, it adopted the so-called *Arusha Declaration*. The declaration, named after the town where it was promulgated, espoused the philosophy of '*Socialism and Self-reliance*' (*Ujamaa na Kujitegemea*). All major means of production were placed under the hegemony of State for the reasons that 'the then private sector lacked both the capacity to generate the needed economic growth and to efficiently allocate resources in a young economy.'<sup>1</sup> And, as UNCTAD correctly puts it, in such an environment competition was considered 'a suspicious capitalist tool' and not 'a developmental tool' of the country's centralised economy<sup>2</sup>.

The days of fuelling socialist ambitions, however, did not last long. From the mid-1980s and early 1990s onwards, several factors contributed towards Tanzania shifting its political stance. These include: a costly war with Uganda, rising prices of oil globally, a shrinking world economy and the fall of the Cold War curtains.

The country's political and socio-economic landscape underwent a surgical metamorphosis embedded in the so-called National Economic Survival Programme (NESP) (1981), followed by 1982 Structural Adjustments Programmes (SAP) and the Economic Recovery Programmes (ERPs). In their totality, these IMF-World Bank backed reforms forced

the government to bid farewell to the socialist policies it had embraced in favour of market-led economic policies.

The parting with the old in order to embrace a new policy orientation was an inevitable event. The country's economic growth at the time was unsustainable and crumbling. Moreover, the monopoly of the public entities, nepotism, and corruption had worsened, and the country was experiencing a low economic growth rate, high inflation and foreign exchange crisis. Coupled with other inefficiencies, all these had brought its economy to a near total market failure.<sup>3</sup> The bottom line, however, was the recognition that a public sector-led economy embodied with restrictive investment climate was unhealthy.

Consequently, there arose a demand for changes; and, changes that would not only bring to the front the noble role, which the private sector could play in promoting sustainable economic growth, but also the rightful breathing space for this sector in the economy. Embarking on a policy re-think to create a fertile regulatory environment designed to correct market failures, was thus an inevitable option. One essential element of that 'fertile and enabling environment' was a sound, fair and transparent regulatory framework in which an effective competition regime became its crucial pillar.<sup>4</sup> Such a noble realization, therefore, called for serious reforms meant to spur the country's economic growth.

## **Regulatory Reforms as a Baseline for Sustainable Growth**

Sustainable economic growth is a function of reforms which include regulatory reforms. As noted earlier, regulatory reforms in Tanzania begun with relinquishing the State's economic hegemony by embracing policies in the nature of liberalisation and privatisation of the erstwhile State owned enterprises. 'Liberalisation aimed at inviting private sector participation in economic development activities, coupled with attracting more Foreign Direct Investment (FDI) in the country, hence more competition.'<sup>5</sup> It involved creation of institutions, laws, regulation and procedures that are consistent and compatible with the market-led economy, and, collectively, they created the requisite environment for investment and sustainable growth of the various sectors of the economy.

Overall, the importance of such reforms and the environment they have created cannot be emphasised. They have continued to assist in minimising costs of doing business in order to stimulate investments, promote industrialisation, and ultimately providing new employment opportunities that add to stability and the total socio-economic and political welfare.

From a competitiveness perspective, the adoption of competition law and policy was a step further in the reform process. This is essentially so because liberalisation and privatisation policies could not alone bring about the desired benefits in the absence of an environment that fosters competition among various economic players. Such a policy choice has witnessed the formation of relevant competition regulatory structures and operational entities, executive agencies, and privatisation of commercial activities that could be carried out in a best way and competitively by the private sector.

The government has since then disentangled itself from the monopoly of public entities in such sectors like telecommunications, allowing competition to flourish for the common good of the nation and the entire public. Instead of being a key player in the market, it has assumed a facilitative role rooted within its mandate to create and sustain a requisite environment within which the market economy principles can flourish.

## Government's Role in Moulding Competition Reforms

It is without doubt that, one major role which any government has to play in a liberalised economy is that of providing the necessary services and frameworks needed for the effective operation of a market economy. This economic system, in which the allocation of resources is determined solely by the forces of supply and demand, needs proper guidance and operational frameworks which, in the context of economic development, ably gauge not only the parameters within which socio-economic activity takes place but also the provision of public goods; regulation of economic activities; reallocation of resources; and stabilisation of the economy.

For its better tailoring, the Tanzanian Government had to set in motion the necessary reforms to remove controls that were earlier set under the *Ujamaa* era. Having so decided, policy makers and the legislature were persuaded to promulgate pro-competition policies and enact laws providing for checks and balances in the market economy. Most of the *post-Ujamaa* legislation enacted focussed, primarily, on not only establishing the legal status of business enterprises and ensures the right and protection of private ownerships (this being a key factor in encouraging entrepreneurship within a country's borders),<sup>6</sup> but also promoting competition by taking suppressive measures against anti-competitive agreements, abuse of dominance, as well as to regulating mergers and acquisitions which result in distortion of the market. One such legislation was *the Fair Trade Practices Act, 1994*.

Essentially, the Act laid down various general competition rules governing anti-competitive activities. Under the Act, anti-competitive practices could not be justified if they significantly affected competition in a market.<sup>7</sup> Basically, the Act covered four main areas; namely:

1. Restrictive business practices,(including those with horizontal and vertical nature);<sup>8</sup>
2. Misuse (abuse) of market power;
3. Control of monopolies and concentration of economic power through mergers and acquisitions;<sup>9</sup> and
4. Consumer protection.<sup>10</sup>

In order to ensure a smooth riding, however, the Government reviewed the Act in 2001 and opted for a two pronged approach to effective regulatory reforms, namely: *economic regulation* and *competition regulation* approaches. The government's role in the reform process may thus be viewed from, but should not be limited to these two approaches.

### **Economic Regulation**

While recognising that competition reforms and the culture of competition need to be well entrenched philosophies in the economy, the government was attentive to the fact that certain sectors of the economy need specific form of regulation. In this regard, the government created separate institutional and legal frameworks apart from the competition regulation framework.

The need to execute change was due to the fact that the first competition regime, established by the *Fair Trade Practices Act, 1994*, was beleaguered with shortcomings that called for its repeal and a new Act was passed for a better focus that separated economic regulation from competition regulation. This re-enactment of the competition regime, led to the passing of four legislative enactments for economic sectors from which the application of the Competition Act was not directly envisaged. The respective legislative enactments which limit the application of the Competition Act are:

- (i) The Energy and Water Utilities Regulatory Authority (EWURA) Act, 2001
- (ii) The Surface and Marine Transport Regulatory Authority (SUMATRA) Act, 2001
- (iii) Tanzania Civil Aviation Authority (TCAA) Act, 2003
- (iv) The Tanzania Communications Regulatory Authority (TCRA) Act, 2003



It is worth noting, however, that these four pieces of legislation regulate certain forms of competition in the respective sectors in which they apply. While they provide that the Authorities will ensure effective competition in the sectors and will investigate anti-competitive conduct, they have the option to refer any anti-competitive conduct in their respective sector to the FCC for investigation. The structure created by these legislations, however, is unfavourable as it complicates effective handling of competition matters as it will be discussed later.

### **Competition Regulation**

One of the rationales for the crafting of a competition law and policy in Tanzania was the need to ensure that former state monopolies, and which were now in the hands of private operators, do not turn themselves as private monopolies. Considering this, governmental policy direction with regard to competition policy is bent towards allowing competition to regulate the market and, where competition is not available and natural monopolies exist, then, some sort of administrative regulatory oversight is available, especially where benefits are seen to out-weigh the costs of regulation. Indeed, as noted earlier, with the exception of the four regulated sectors, (mostly utility sectors) the rest of the economic sectors fall within the ambit of competition regulation.

Following the need to re-shape the initial competition regime established under the 1994 Fair Trade Practices Act, the prevailing law on competition has been the Fair Competition Act, 2003. This Act replaced the 1994 enactment.

The Act has established a fully functioning and independent Commission as a market support institution responsible for addressing anticompetitive conduct in the market, and a Tribunal which determines appeals arising from the decision of the Commission. The presence of the Commission and the Tribunal in place to address fair play in the Tanzanian market, offers a wealth of market opportunities for both to internal and foreign companies.<sup>11</sup>

Generally, the Act and its enforcement machinery provide an environment which not only guarantees for a fair exit from but also free entry into the market. Such an environment provides for the conditions necessary for fair competition and sound operations among the various players in the economy, thereby adding flavour to the designation of Tanzania as an attractive investment destination.

Currently, 'with a population of [over 40mn] consumers, a rapidly growing economy, and high levels of domestic investment spending, the Tanzanian market remain[s] an important target destination for local and

foreign products and services.’<sup>12</sup> All these signify the benefits, which the regulatory and competition reforms can bring and which has the impact of not only alleviating poverty and increase investment and employment opportunities but ultimately spur sustainable economic growth.

## **Competition Policy and the Participation of the State in the Economy**

As already noted in 3.0 above, the role of State in promoting competition cannot be over emphasised. Notwithstanding this fact, in a country like Tanzania, where hitherto the State had an upper hand in the market through public corporations and institutions that regulated prices, for example, the National Price Commission,<sup>13</sup> there are few instances when the State might act as a stumbling block to effective competition. This might, especially occur where the State interferes with the effective functioning of competition in the market place through the so-called state-related restraints. Such state-related restraints may appear in various forms including, but not limited to state’s ownership of shares in public corporations or granting preferential privileges or protection to certain entities ‘national champions’ as compared to others plying in the same market.

In Tanzania, the framers of the Fair Competition Act did consider the interplay between the introduction of competition policy and the participation of the state in the economy. To be precise on this, section 6 of the Fair Competition Act (FCA) is a relevant provision to refer to when dealing with the State’s involvement in the market. The section provides as follows:

- ‘6.-(I) This Act shall apply to Mainland Tanzania, state bodies and local government bodies in so far as they engage in trade.
- (2) Notwithstanding the provisions of sub-sections (1), the State shall not be liable to any fine or penalty under this Act or be liable to be prosecuted for an offence against this Act.
- (3) For the purposes of this section, without affecting the meaning of ‘trade’ in other respects -
  1. The sale or acquisition of a business, part of a business or an asset of a business carried on by the State, a State body or a local government body constitutes engaging in trade; and
  2. The following do not constitute engaging in trade:
    - (i) the imposition or collection of taxes;

- (ii) the grant or revocation of licences, permits and authorities;
- (iii) the collection of fees for licences, permits and authorities;
- (iv) Internal transactions within the Government, a State body or a local government body.'

As it may be seen from the above provision, the interplay between the introduction of competition policy and the participation of the State in the economy is limited only to the extent which the State bodies or local government bodies are actively engaged in 'trade.' Although the Act defines the term 'trade', under section 2, as including 'commerce', this definition is not sufficiently elaborate. Nevertheless, from common knowledge, the term 'trade' may be regarded involving the 'intercourse for the purposes of trade in any and all its forms, including the transportation, purchase, sale and exchange of commodities.'<sup>14</sup>

Considering what section 6(1) of the FCA provides, where a government department or a local government engages in a conduct that amounts to doing business within the context of this provision, it has to abide with the general competition law principles. If the conduct violates the FCA, it will be subject to investigation and sanction under the Act. A good example of a case, which considered the application of section 6(1) of the FCA was the case involving the Tanzania National Roads Agency (TANROADS). This case involved the issuance of exclusive permits to erect gantries and billboards along road reserves sites throughout the country.

The permits were only issued to two firms by TANROADS, fact which made other players in the outdoor advertising market to lodge a complaint at the FCC. While determining the case, TANROADS challenged the jurisdiction of the Commission stating that being a state agency was, by virtue of section 6(2) of the FCA, immune from the application of the Act. However, the Commission was satisfied that since the alleged conduct constituted a barrier to other potential entrants in the same business of advertisements through gantries and billboards, it had jurisdiction to determine the matter and, that, TANROADS fell within the ambits of section 6(1) of the Act.

In the final analysis of the matter, the Commission held that TANROADS was a State body and not the State, hence, not subject to the exemption under the provision of section 6(2) of the Fair Competition Act. Its agreements with the respective firms were declared null and void

for having contravened the Fair Competition Act. All these developments painted a new picture, which reveals that, with a guaranteed independence, a competition authority can still oversee and build a culture of competition and dispense ‘competition justice’ even against State-related agencies or department when such are involved in perpetuating anticompetitive conduct.

## **Unveiling the Policy, Institutional and Implementation Challenges**

It is now more than two decades since Tanzania adopted a competition legal framework and a decade long since the Fair Competition Commission (FCC), as an institution that oversees competition in the market, was established. For all these past years, the path towards a flourishing competitive market economy in Tanzania has not been smooth.

There have been challenging issues ranging from policy, legal and institutional setting, as well as human and financial resources challenges, all making it difficult, though not impossible, to sustainably carry-out the necessary functions of building an environment within which the benefits of competitive market economy could be fully realised.

### **Policy-Legal related Challenges**

As already stated, from 1990s onwards, governmental policy direction with regard to competition policy was bent towards allowing competition to regulate the market. Where competition is not available and natural monopolies exist, then, the government opted for some sort of administrative-regulatory oversight, especially where benefits were considered to be out-weighing the costs of regulation.

Thus, with the exception of the four regulated sectors mentioned earlier, (mostly utility sectors) the rest of the economic sectors should automatically fall within the ambit of competition regulation. While this policy decision by the government was perfect when the country was still crafting its regulatory route the whole scenario, if examined, and its trajectory having been treaded for two decades now, it reveals some challenges that pose a serious threat to a well-functioning competition regime.

Indeed, by creating regulatory institutions with concurrent mandate to deal with certain competition issues in their respective sectors<sup>15</sup>, there has been a loophole that anti-competitive conduct in those sectors may be left unattended. This risk is supported by the fact that, unlike the FCC, the rest of regulatory authorities spend more time and expertise on

technical/economic regulation in their sectors than on competition regulation. The reason for this is simple. They were not established, like the FCC, to specifically address competition issues and, consequently, their expertise on investigations and handling of anti-competitive conduct that may be within their respective sectors is limited.

This is a challenge that necessitates a thorough review of the current policy-cum-legal structure in order to separate economic regulation from competition regulation in those sectors and to allow the FCC to have an overriding mandate on competition issues even in those sectors.<sup>16</sup>

Furthermore, vesting the FCC with direct powers to intervene and investigate anti-competitive conduct in any of the regulated sectors will also help to remove any confusion or uncertainty which may occur should a Regulatory Authority, for instance, pursuant to its enabling Act; punish its subjects for violations of the laws and regulations governing the sector, e.g., cancellation of a license, and at the same time refer an anticompetitive conduct to the FCC for investigation.

In such a scenario, the culprit may rely on the *Ne bis in idem* (double jeopardy) principle to challenge any decision which the FCC may wish to take, hence unnecessarily prolonging the effective enforcement of the competition principles. There is at least an example from our experience, which might assist to illustrate this point better.

Since 2011, the FCC has been pursuing a cartel-related case in the petrol supply industry. The facts of the case are that, because petrol supply sub-sector is a regulated sector, in 2011 the regulator (EWURA) issued a cap price indicating price for which a litre of petrol or diesel was to be sold.

The oil marketing companies, through the Chairman of their association, Tanzania Oil Marketing Companies, 'TAOMAC' issued statements through the media boycotting to supply fuel to the market in opposition to the new cap-pricing regulations. The incident, which seems to have been coordinated through 'TAOMAC', led to disruption in the entire market and occasioned sufferings to consumers and the entire economy for almost three consecutive days.

The regulator issued several compliance orders to some of the members of 'TAOMAC' and referred a complaint against the conduct of both the 'TAOMAC' and its chairperson to the FCC. When the FCC took up the matter and opened an investigation to establish whether the provisions of the Fair Competition Act which prohibits collective boycott by competitors were breached.

Although the matter is yet to be finalised, there has been several objections by the members of "TAOMAC" to the effect that the matter

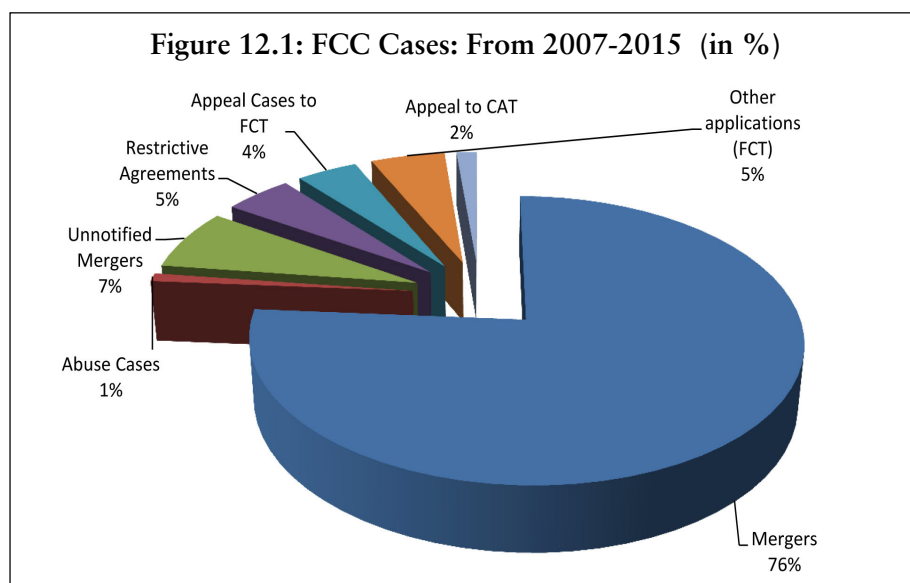
ought to have been dealt with by EWURA, the regulator of the relevant industry, since its establishing law gives it such a mandate. Such sorts of arguments tend to prolong litigation unnecessarily. Their key roots, however, is the underlying policy and legislative framework upon which the whole idea of economic and competition regulation was pegged from its inception.

Since the ‘TAOMAC’ case is still pending, it suffices here to state that, there is a need to vest all mandate relating to overseeing competition and investigating misconducts in an economy to one entity only.

### **Challenges Arising from the Current Institutional Set-up**

The Fair Competition Act, 2003 established a fully functioning and independent Commission as a market support institution responsible for addressing anticompetitive conduct in the market, and a Tribunal which determines appeals arising from the decision of the Commission.

The Commission became operative in 2005, and since then it has dealt with cases ranging from merger applications (158 cases); un-notified mergers (15 cases); abuse of dominance (2 cases), restrictive agreements (10 cases), and 2 exemption cases, all being part of its mandate under the law. The Commission has also defended appeals and applications arising from its decision. There has been (9) appeal cases, (3) of which are still pending at the Court of Appeal of Tanzania) and 11 applications filed at the Fair Competition Tribunal. Figure 12.1 shows the number of FCC’s competition related cases, in percent -wise, received as from 2007 to 2015.



Despite the above noted successes and, although the Fair Competition Act and its enforcement machinery provide for an environment, which not only guarantees a fair exit from but also free entry into the market and; even if this fact adds flavour to the designation of Tanzania as an attractive investment destination,<sup>17</sup> the current institutional design has been, and remains to be open to challenge.

The current design combines investigatory, prosecutorial, and adjudicative functions. This set up has created anxiety among legal practitioners who view it as violating the constitutional principle of separation of powers, even if the Commission's *modus operandi* is inquisitorial in nature.

Under section 69(1) of the FCA, read together with Rule 10(2) of the Fair Competition Procedure Rules, for instance, the Commission can initiate a complaint on its own and can investigate the same and make a finding. In 2010, in *TCC v FCC*,<sup>18</sup> an attempt was made to challenge this provision at the High Court of Tanzania testing its constitutionality.

The Court, however, dismissed the petition on a technicality without entertaining the matter on the merits since it was wrongly moved by the petitioner. An appeal was preferred to the Court of Appeal and the same has not been determined. Viewed from this perspective, one would envisage a need to re-examine the current institutional set-up lest we find ourselves in a messed-up situation like the one in which the Jamaican Fair Trading Commission was thrown into following the decision of the Jamaican Court of Appeal in *Jamaican Stock Exchange Commission v Fair Trading Commission (FTC)*, Supreme Court Civil Appeal No.92/97. In this case, it was held, *inter alia*, that it was improper for the respondent (FTC) to perform the functions of a complainant and adjudicator since that was in breach of the principles of natural justice.

Taking the above example and, given the attempt to challenge section 69(1) of the FCA, there still remains a looming challenge that hangs on top of the to the FCC as the sword of Damocles. Indeed, if successfully pursued in view of the pending appeal in the Court of Appeal of Tanzania, the decision may paralyse the carrying out of the functions of the Commission.

In view of this, and as once noted elsewhere, since “[a] regulatory framework should clearly, appropriately and sufficiently address ‘how’ the regulatory functions are to be carried out – the processes and governance arrangements - particularly as they pertain to agencies established to carry out regulation of a sector or market area;”<sup>19</sup> then, there may be a need to re-consider the current set-up of the Commission.

Although it is established that the Commission conducts its business through an inquisitorial process (as opposed to the adversarial process), one proposal, which may be taken up for consideration in order to ensure separation of investigation and adjudicatory powers within the Commission is to broaden the number of the Commissioners and limiting the involvement of the Director General (DG) in the decision making process.

Instead of having the DG as a Commissioner who sits in the case meeting, the Commission may create a committee of experts in which the DG will sit (since he heads the secretariat, i.e. the Director General and his management team of technical experts) and the Commission should delegate powers to such a committee, tasking it with the responsibility of conducting *preliminary hearing of the cases* and *making preliminary assessments/ provisional findings of investigations* for recommendation to the Commission.

In my view, such a division of responsibilities between *the Commission* and *the Secretariat*, which is headed by the DG, will ensure that there is fairness and objectivity in the operations of the Commission and also that there is a separation of powers between investigations and case adjudication. Otherwise, the FCC may remain a purely investigatory body while the FCT handles all adjudicatory issues arising from the investigations conducted by the FCC.

It is also worth noting that the FCC handles consumer complaints as well. The Commission, however, has been unable to address consumer complaints effectively since most of the current provisions of the FCA do not give the Commission power to punish the culprits who violate the relevant consumer protection principles.

In most cases the FCC ends up advising consumers to resort to the ordinary courts for redress, and, as well understood, such a route is less favourable given the length of time, which a case may take in a court and expenses that may be involved until one gets the requisite redress. To address this shortcoming the FCC has proposed for the amendment of the current law so as to allow the Commission to act as a small claims court and also apply the alternative dispute resolution (ADR) mechanisms in dealing with consumer complaints.

### **Challenges Arising from Lack of Sufficient Financial and Human Resource**

As depicted earlier on the historical overview of the competition regime in Tanzania, competition was not a culture experienced in the country but a 'new baby in town.' In view of this, more efforts to build a culture



of competition among players have been an essential agenda from the time when the FCC became functional.

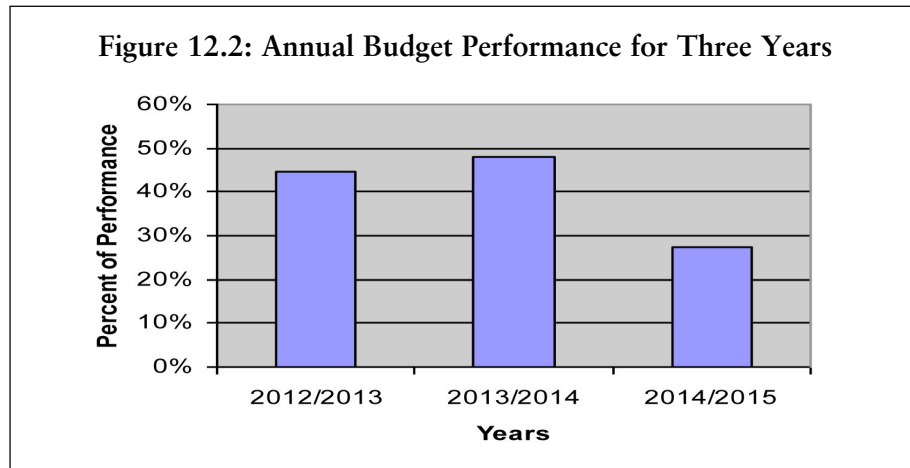
This FCC's agenda has to be implemented through competition and consumer advocacy campaigns. The success of this strategy however, has been starved by inadequate funding since the FCC is not fully funded by the government. The FCC is a business support and not a business making institution. According to section 78 of the FCA, it is provided that Funds of the Commission will comprise of -the (a) fees not exceeding 2.5 percent of business licenses; (b) any grants, donations, bequests or other contributions made to the Commission; (c) funds allocated to the Commission from the Regulatory Authorities, (d) funds allocated to the Commission by Parliament; (e) fees collected by the Commission; and (f) all other payment due to the Commission in respect of any matter incidental to its functions.

Despite these sources being well noted by the Act, they have remained undependable sources and funding the business of the Commission has remained a hard nut to crack.

The current arrangement with the regulatory authorities mentioned under the Act is for them to fund the budget of the FCC on *pro-rata* basis. While the FCC submits its proposed budgets well in advance and carries out consultative meetings with the relevant regulatory authorities (RAs), the agreed *pro-rata* mode of remittances from the RAs has never been effective.

The FCC's requests for funding from the relevant RAs pursuant to the available funding regulations made under section 78 of the FCA has never been remitted 100 percent as requested. In summary, Table 12.1 shows a comparative annual Regulatory Authorities budget performance percentage view for three financial FCC years 2011-2012 to 2014-2015.

Table 12.1: Annual Regulatory Authorities Budget Performance Percentage (2012-2015) – Amount in Million Tanzania Shillings				
Year	Request	Disbursed	Percent Deficit	Percent Performance
2012/2013	2,707	1,209	55%	45%
2013/2014	2,585	1,238	52%	48%
2014/2015	3,298	900	73%	27%



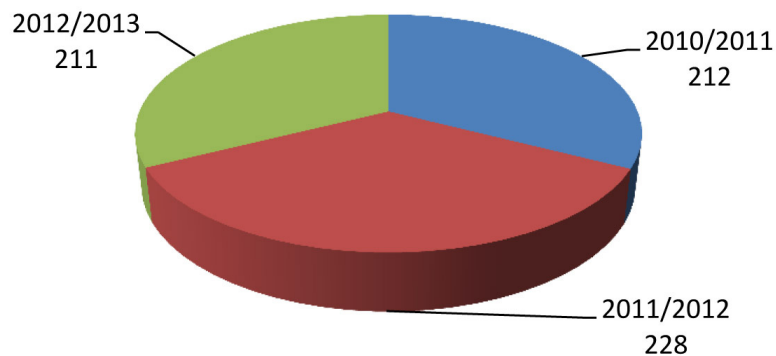
As it may be seen from the three years analysis shown in Table 12.1 from 2012-2015 the Commission budget from Regulatory Authorities has never been achieved by more than 50 percent. In the year 2012/2013 it was achieved by 45 percent followed by 48 percent in the year 2013-2014 and 27 percent in the current year 2014-2015. These variations have had a negative impact on Commission's achievement of its objectives, goals, targets and activities due to the fact that the Commission had to drop some of its planned activities due to financial difficulties.

This challenge is further complicated by the fact that, although the FCA provides for an allocation of equal to 2.5 percent of fees charged from business licenses by local authorities, nothing has ever been remitted to the FCC. In view of all this, one can imagine how frustrating it may be when a competition authority is poorly funded. Even if it will plan, it will not manage to carry out all its plans successfully.

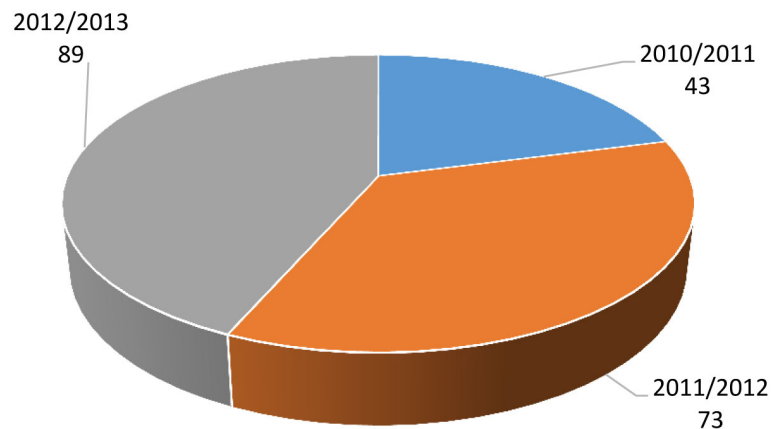
It must be noted that 'effective implementation of competition law needs to be secured through sufficient funding'<sup>20</sup>. For that reason, the Government needs to appreciate and practically addressed the funding issue since the FCC is an important institution to the economic well-being of Tanzania.

It is also worth noting that, apart from dealing with competition issues, the FCC is also mandated to fight counterfeits from the market and protect consumers. Up to the moment it has been able to confiscate and destroy counterfeit products worth approx. Tanzanian Shillings 5 billion. The figures 3 and 4 below illustrates what was done over the past three financial years, 2010-2011; 2011-2012 and 2012-2013.

**Figure 12.3: FCC's Implementation of Its Anti-Counterfeit Mandate in 2010-2013**



**Figure 12.4: Number of Raids Conducted**



Another resource-related challenge which the FCC has been facing relates to inadequacy of its manning levels. Since its inception to-date the Commission has not been able to attain its full manning level.

This has an implication on its overall performance given that the Commission (as an entity) discharges another separate mandate (through the Director General as the Chief-inspector), of dealing with counterfeit goods. Although it is well known that the FCC can recruit its own members of staff, the other flip side to this fact is that payment of personal emoluments to such staff members is a function of the central government given that all staff members are public servants in the public service.

This means there must be a permit to recruit from the central establishment, (the Permanent Secretary Public Service Management) and, such permits are often not easily issued especially because the interest of the central establishment to recruit personnel might be in respect of other areas, which are considered to be of priority. As a result, the Commission fails to carry-out its mandate fully.

### **Challenge Resulting from the Risks of Regulatory Capture**

As noted earlier, the adoption of market economy in Tanzania involved privatisation of the erstwhile public entities and opening up various sectors to competition. It is clear, however, that most influential people in politics and business became shareholders in most of the privatised entities and, since such entities had been enjoying less competition they would wish to continue with such a state of affairs even after the new form of competitive environment had come into the scene. That being the case, one of the challenges that face most young competition authorities is the possibility of succumbing to the regulatory capture syndrome<sup>21</sup>.

In such a scenario, politicians tend to use their political influence to interfere with the exercise of regulatory mandate vested on the competition authority, for instance, with regard to mergers and acquisitions considered to be anti-competitive. To do so, they will do all they can, using their political offices or influence, to instill pressure on the competition authority whenever the authority takes a bold step to investigate alleged anti-competitive conduct against them, with a view to make the authority lose sight of the public or consumer interests it is supposed to safeguard and protect the privileges of the particular firm in question.

One example, in our case, is a complaint concerning un-notified merger and abuse of dominance which the Commission pursued against a dairy milk processing plant, *Tanga Fresh Ltd* (TFL) from 2010 to 2015. In 2009, TFL acquired two of its competitors without first filing a notification before the FCC.

When the Commission learnt of the transactions and initiated an investigation in accordance with the provisions of the FCA, TFL, through one of its shareholders, Tanga Dairy Cooperative Society, resorted to political offices for salvation. The matter was brought to the attention of a parliamentary committee responsible for trade, industry and economic affairs and certain officials from the FCC were summoned to appear before the committee.

Even so, the FCC was adamant in ensuring that the law is properly adhered to and issued its final decision on the complaint, which was upheld

by the Fair Competition Tribunal upon an appeal preferred by Tanga Fresh Ltd. This is one of the cases that exposed the FCC to the risks of regulatory capture, a fact which is still alive to most young competition authorities, especially due to the reason that the culture of competition has not sunk deep within the fabrics of the society. However, as once stated, competition authorities doing their job properly should always resist such pressures.<sup>22</sup>

### **Challenges Resulting from Lack of Sufficiently Entrenched Competition Culture**

‘A ‘culture of competition’, is the desirable situation that exists within a country when the rules and benefits of competition are widely known and supported, and where serious consideration of the likely impact of actions and regulations on competition forms a natural part of the background for decisions by firms and governments. Building a culture of competition and an effective competition regime is a long-term endeavour, and not just a matter [of] one-off events. Competition must be ‘mainstreamed’ in all sectors.’<sup>23</sup>

Lack of sufficiently rooted culture of competition within a developing economy like Tanzania, and given its socio-economic and political history explained above, creates another barrier to successful discharge of functions vested on the FCC. The Commission has been facing obstacles, for instance, in accessing bills meant to be tabled before the parliament for its prior review in order to ensure that the envisaged legislation does not become a barrier to competition.

Resistances have also been noted in sectors such as insurance where a prudential regulator of the sector wants at the same time to assume the role of regulating anticompetitive conduct unveiled by the Commission. A case in point is one involving two insurance associations, the Association of Tanzania Insurers (AIT) and the Association of Insurance Brokers (AIB).

The two colluded and fixed motor vehicle premium rates to be charged by their members. When the matter came to the attention of the FCC, as the conduct is prohibited under the FCA, the insurance regulator challenged the FCC before the Attorney General (AG) alleging that the proper entity to deal with the matter is not the FCC but itself. Since 2013 the matter has been unattended as the AG is required to issue guidance as the Chief advisor to the government on matters of law.

Looking at the whole issue, however, the only conclusion which can be drawn is that the current tussle between two government regulatory

entities is that there is still a lack of sufficiently rooted knowledge and culture of competition within the sectors of the economy, a fact that calls for more advocacy sessions to government entities by the Competition authority as part of the corrective measures.

### **The Challenge Emerging from the Lack of Functioning East African Competition Authority (EACA)**

As it may well be known, regionally within the East African Community there is a law to govern competition issues and protect consumers. However, the Act has largely remained ineffective because some of the member States to the community are yet to domesticate it. Due to this fact, the envisaged EACA has not been functional and cross-border mergers tend to be notified in all countries under the respective domestic laws.

Even if the authority was to be functional, there still remain unanswered questions regarding whether a merger with cross-border effect will still need to be notified in the jurisdiction where it has its nexus or should only be notified to the authority. Whether and at what rate should part of the notification fees payable trickle down to the national competition authority from the regional authority is yet another unsolved issue. It suffices here to note that all such issues are challenging since some national competition authorities partly fund their activities through fees payable by notifying parties.

## **Conclusion**

Ever since the time when Tanzania embarked on the competition reforms' process, the role which competition policy has been playing in the economy in terms of promoting healthy markets, consumer welfare, employment, innovation and industrialisation, is significant. Briefly stated, the reforms have opened plenty of opportunities for investments and economic growth.<sup>24</sup>

Notwithstanding this fact, it is worth emphasising that competition policy is not, on its own, a panacea for a sustained economic growth. Strong political commitment that seeks to promote and sustain on-going regulatory reforms is still required on the part of the Government and its various agencies if Tanzania is to leap frog from a low to middle income before 2050. This is essentially the case because successes or failures of competition reform, or any regulatory reform, depend on the political will of the government of the day.

As noted from the above discussion, the competition regime in Tanzania is still faced with challenges that need to be addressed. Whereas the structural design challenges that are hinged on the establishing legislation may be addressed through amendments, other challenges such as poor financing of the FCC are policy related matters that need to be taken up by the government itself if at all it is strongly committed to reforms and ensuring that a culture of competition permeates within the entire economic fabrics of the society.

In our view, the first and foremost commitment which the government needs to portray is strong and consistent support to the institutions vested with the mandate to provide competition regulation oversight. Governmental funding is a crucial support that must be given to the authority. As noted in this discussion, while the FCC's operational budget has been growing perpetually, its financial support has been gradually diminishing.

This tendency tends to reduce the necessary independence which a competition authority needs to maintain. Lacking sufficient funding has the potential to weakening the position of the agency and reduces its visibility, relevance, and voice within the nation. It makes it difficult for the agency to air its views or to be heard at the Governmental or political levels because, important activities, such as advocacy, which could have enhanced its visibility are not fully carried out.

Consequently, the agency becomes less or rather consulted late in all processes relating to policy or legislative formulations, which, as a matter of fact, ought to be scrutinised to ensure that they do not create barriers to competition.

It is also worth noting that there are still grey areas which need to be further explored for the sole purpose of captivating not only the culture of competition within the various sectors of the economy but also the entire rationale for competition reform agenda.

Since it is agreed that competition among various players in the economy has the potential to spur sustained economic growth there is now a need to ensure that the would-be barriers to competition, be they artificial or statutory are completely removed so as to ensure not only free movements of goods and services but also effective enforcement of the competition law by the respective machineries.

In this regard, the FCC has, for instance, come up with a strategy to engaging with various government departments and agencies and regulatory bodies through entering into Memorandums of Understanding (MoUs), which aim at not only ensuring that the relevant governmental departments, agencies or regulatory entity lend support to the effective

carrying out of the Commission's mandate but also ensuring that the culture of promoting competition permeates into their daily operations.

Finally, we wish to express our views that, in order to realise the highest returns from competition or any other regulatory reforms, apart from addressing key challenges as those enlisted herein, above, participation of key competition stakeholders in the reform process and those who are beneficiaries of the reforms, is vital. This entails enhancing the role of competition and consumer protection advocacy at national and regional levels including, but not limited to holding regional and national consultative meetings with the business community, investors, consumer groups, governmental departments and ministries with a view to disseminate the competition gospel thus winning their support for any of intended future reforms.

Effective involvement of such key players is essential in not only building or strengthening the requisite synergies that exists or that need to be established but also helps to promote the enjoyment of a continued support for the competition reform agenda within the given country or regional economic grouping.

It is further argued that building or strengthening existing synergies between regulatory institutions, relevant government agencies, and stakeholders or players in the business circles, is vital since it enhances the chances of instilling the competition philosophy and culture within and among key players within a given market.

In particular, key reforms in the other areas such as the area of governance, are vital ingredients for a sustainable economic growth. Such reforms include, but are not limited to, reforms geared at enhancing cost-effective measures such as reducing (and completely) eliminating corruption, mismanagement of resources, enhancing efficiency in service delivery, increasing consumer awareness of and their voice against inefficiency costs in various service delivery sectors such as ports, airports, tax revenue offices, and licencing authorities, as well as improving coordination and transparency among various government agencies and stakeholders.

All these elements have the potential to contribute to sustainability and economic growth because they have the potential to spur investments, both local and freeing direct investments, enhances the ease of doing business, promote trust and confidence in the underlying economic systems, such as financial as well as operational systems in a given country, thus ultimately promoting more competition in the economy, poverty reduction, unemployment as a result of improved welfare and societal development.



## Endnotes

- 1 See: Waigama, S.M.S, *Privatization Process and Asset Valuation: A case study of Tanzania* (unpublished PhD Dissertation, School of Architecture and the Built Environment Royal Institute of Technology Stockholm (2008) at 1.
- 2 See: UNCTAD, *Voluntary Peer Review of Competition Law and Policy: A Tripartite Report on the United Republic of Tanzania- Zambia-Zimbabwe*, United Nations, New York and Geneva, (2012) at 38.
- 3 It is noted, for instance that , in ranking of the world's poorest countries, the position of Tanzania changed dramatically in the 1980s dropping from 14th poorest in 1982, with a GNP per capita of \$280, to the 2nd poorest in 1990, with a GNP per capita of US\$110. In previous years, particularly the 1960s and 1970s, real GDP per capita was growing at an average annual rate of 1.5 - 1.9%. However in the period between 1981 and 1986, it registered a negative annual growth rate of 2%. See: Ministry of Industry and Trade (MIT), "Analysis of the Services Sector with a View to Making Commitments in the Context of Trade Liberalization at Bilateral, Regional and Multilateral Trade Negotiations: The Case of Tanzania" at p.11 (available from <http://www.tzonline.org/pdf/analysisoftheservicessector.pdf> (as accessed on 24/6/2015)).
- 4 See: Sengupta, R and Mehta, U.S, 'Competition Reforms – An Essential Element to Evolving a Sound Business Environment in Eastern and Southern Africa 'CUTS International, India (available from <http://www.businessenvironment.org/dyn/bel/docs/154/Sengupta.pdf>, at 1.
- 5 MIT (op. cit. note 3) at page 12.
- 6 See: for instance, the enactment of Land Act, 1999 (Cap 113); the Village Land Act, 1999 (Cap 114) and the Unit Title Act of 2008;the Business activities registration Act 2005; The Business Names (Registration) Act (Cap. 213); Tanzania Revenue Authority Act 2006and the Tanzania Investment Act, 1997 .
- 7 See: CUTS, *Competition Law and Policy: A Tool for Development in Tanzania* CUTS Centre for International Trade, Economics & Environment, (2002) at 30.
- 8 These were dealt with under section 15 to 29 of the Act.
- 9 These were dealt with under section 30 to 40 of the Act.
- 10 See Sections 51-93 of the Act.
- 11 See: Musiba, E., 'Reforming the Business Environment in Tanzania' (available from <http://www.businessenvironment.org/dyn/bel/docs/83/Session5.2MusibaDoc.pdf> (as accessed on 22/6/2015)).
- 12 Ibid.
- 13 This was established under the Regulation of Prices Act, (Act No. 19 of 1973) and was vested with powers to administer a price control system. The Act has since 1994 been repealed.
- 14 See: *Welton v Missouri* 91 US 275 (1875) per Filed, J. See also *Ranson v Higgins* [1974] 1WLR 1594 at 1600; *Re Ku-ring-gai Co-operative Building Society (No 12) Ltd* 36 FLR 134 at 139.
- 15 See, for instance, section 20 of The Energy and Water Utilities Regulatory Authority Act, 2001; Section 19 of Authority Act, 2001 The Surface and Marine Transport Regulatory Authority Act 2001; Section 25 and 40 of the Tanzania Civil

Aviation Authority (TCAA) Act, 2003; and Sections 5 and 19, 65 of Tanzania Communication Regulatory Authority Act, 2003.

- 16 It is crucial to note that for the past one decade of its presence and of dealing with competition issues, the FCC has built its expertise in the area even if the journey to the mastery of competition issues is yet to be attained in full.
- 17 Ibid. The author notes that currently, ‘with a population of [over 40 million] consumers, a rapidly growing economy, and high levels of domestic investment spending, the Tanzanian market will remain an important target destination for local and foreign products and services.’ All these signify the benefits which the regulatory and competition reforms can bring and which has the impact of not only alleviating poverty and increase investment and employment opportunities but ultimately spur sustainable economic growth.
- 18 Misc. Civil Petition No.131 of 2010, High Court of Tanzania, (Unreported).
- 19 “PPIAF – Jamaica Regulatory Impact Study Legal Gap Analysis, Report (2006), Cambridge Economic Policy Associates Ltd In association with The University of West Indies (UWI) (available at <http://www.ppiaf.org/sites/ppiaf.org/files/documents/Jamaica-legal-gap-analysis.pdf> (as accessed on 2/9/2015)).
- 20 See UNCTAD, Voluntary Peer Review Of Competition Law And Policy: A Tripartite Report on The United Republic of Tanzania- Zambia-Zimbabwe, United Nations, New York and Geneva, (2012), at 82.
- 21 The concept of regulatory capture was introduced by George Stigler and Sam Peltzman. For a brief description see Kip Viscusi, John Vernon and Joseph Harrington Jr. (2000), *Economics of Regulation and Antitrust*, The MIT Press, Cambridge, Massachusetts, Third Edition, pp. 317.
- 22 See: Advocacy and Competition Policy: Report Prepared by the Advocacy Working Group ICN’s Conference Naples, Italy, 2002, at pp. 28-29.
- 23 See: Preston, J. ‘Implementing Competition Policy in Developing Countries: The Role of Donors’ International Conference on ‘Reforming the Business Environment – From Assessing Problems to Measuring Results’ Cairo: 29 November – 1 December 2005, at p.13. (Available from: <http://www.businessenvironment.org/dyn/be/docs/80/Session3.4PrestonDoc.pdf> accessed on 25/3/2014)).
- 24 See: generally, Wangwe, S.M. ‘Economic Reforms and Poverty Alleviation in Tanzania’, ESRF- ILO Paper No.7, (1996) (available from [http://ilo.org/wcmsp5/groups/public/-edema/documents/publication/wcms\\_125479.pdf](http://ilo.org/wcmsp5/groups/public/-edema/documents/publication/wcms_125479.pdf) (as accessed on 23/06/2015)).

# 13

## Two-Sided Markets and their Impact on Economy

### *Cases from India*

VARADHARAJANAN SRIDHAR  
*Associate Professor*  
*Department of Chemistry and Bio-Chemistry*  
*Bombay University*  
*India*

#### **Abstract**

The Internet companies, often referred to as Over-The-Top (OTT) firms have powered ‘sharing economies’ around the world (Weber, 2014). Two Sided Markets (2SM) and associated Platforms form the basis of operation of these firms. In a typical 2SM, there are two sets of users who complement each other’s usage thereby increasing the network effect for enhanced value for both<sup>1</sup>. Often, one side of users cannot exist without another and a platform is possibly the only way for them to efficiently get to know each other and transact commercially. India is unique in this aspect, compared to many other countries since a large number of unorganised set of firms exist and that too especially in direct consumer related verticals, such as travel, consumer goods, healthcare, apparel, fashion, to name a few.

India is also witnessing for the first time a deluge of ideas and 2SM based start-ups coupled with an ensemble of angel investors, incubators and accelerator. Part of this enthusiasm is due to improved adoption of computers, mobiles, and smartphones and the increasing penetration of mobile Internet broadband across the length and breadth of the country. However, in India as in other developing countries, there are considerable challenges to interconnect the two sets of users and that is where the

value of platforms, such as the above comes out. The paper provides taxonomy of such 2SM platforms in existence, especially in India, their economic and social benefits, the competition effect, and the associated regulatory and policy interventions.

## **Introduction**

The Internet companies, often referred to as Over-The-Top (OTT) firms have powered 'sharing economies' around the world<sup>2</sup>. Two Sided Markets (2SM) and associated Platforms (P) form the basis of operation of these firms. In a typical 2SMP, there are two sets of users who complement each other's usage thereby increasing the network effect for enhanced value for both<sup>3</sup>. Typical examples include an e-commerce portal that connects users on one side with suppliers of goods on the other side; a travel portal that intermediates between travellers on one side and the travel firms on another; and so on.

Often, one side of users cannot exist without another and a platform is possibly the only way for them to efficiently get to know each other and transact commercially. This becomes very important, especially in an unorganised sector where it is of prime importance for the platform provider to bring a semblance of organisation, thus facilitating commerce between the two sets of users.

India is unique in this aspect, compared to many other countries since a large number of unorganised set of firms exists and that too, especially in direct consumer related verticals such as travel, consumer goods, healthcare, apparel, fashion, to name a few. The growth of 2SMPs, though not new, is fuelled by the proliferation of Information and Communication Technologies (ICTs). ICT parameters for India are given in Table 13.1.

Though the Network Readiness Index has not progressed much and the country is still ranked in the 89<sup>th</sup> position out of the 140 countries in WEF (2015), there are some distinguishing characteristics. The mobile subscriber base in India is the second largest in the world and the mobile networks cover more than 90 percent of the country's population.

Though Internet and broadband penetration is still low, more and more of users access Internet only through their mobile devices. The start-up eco system in the ICTs is very vibrant in the country, as exhibited by the venture capital availability. Bangalore, India is rated consistently in the top 20 global start-up ranking, along the leagues of Silicon Valley in the US. Though the impact of ICTs on new products and services is still evolving, it is still consistently ranked above 4 (scale 1-7) indicating its potential.

<b>Table 13.1: ICT Data of India (as on Dec 2014)</b>	
Network Readiness Index (WEF, 2015)	3.7 (scale 1-7)
Mobile subscriber base (in Million)/ Mobile density per 100 population	930.20/74.55
Number of Internet Subscribers (in Million): Wireline/ Wireless	18.70/235.70
Number of Broadband subscribers (in Million) (Wireline/ Wireless)	15.13 /60.60
Impact of ICTs on new products and services (WEF, 2015)	4.1 (scale 1-7)
Global start-up eco system rank: Bangalore, India (Compass, 2015)	15 (out of Top 20)
Venture capital availability (WEF, 2015)	20 (Rank out of 143)
Laws relating to ICTs (WEF, 2015)	3.9 (scale 1-7)

India is also witnessing for the first time a deluge of ideas and 2SMP based start-ups coupled with an ensemble of angel investors, incubators and accelerator. Part of this enthusiasm is due to improved adoption of computers, mobiles, and smartphones and the increasing penetration of mobile Internet broadband across the length and breadth of the country. Part of it is also due to the inherent inefficiencies of the current unorganised sector and a possible solution in an organised 2SMPs.

However, in India as in other developing countries, there are considerable challenges to interconnect the two sets of users and that is where the value of platforms becomes important. On the other hand, due to relatively low entry barriers, it is easy to set up the platform business, and hence, the reason for hundreds of start-ups in this space.

The caveat is that until the two sides scale up considerably the value of the platform remains minimal. In the following section, the theory and characteristics of Two-Sided markets and platforms will be discussed; in the subsequent section, we provide five case studies from different areas of the Indian economy and illustrate their evolution and benefits for the two sets of users; in the concluding section, provide indicative policy steps for addressing these markets.

## Theory of Two-Sided Markets and Platforms: A Literature Review

This Paper extends the principles of Appropriate Technology and Fortune-Seeking from the Bottom of the Pyramid expounded by Kumar & Du (2011). Through cases, this paper attempts to bring out the socio-economic impacts of ICT enabled 2SMPs.

‘Network externalities’ are qualities of certain goods and services such that they become more valuable to a user as the number of users increases. Examples of products exhibiting network externalities include fax machines, credit card networks, telephone services, broadcast industry services, computer hardware and software<sup>4</sup>.

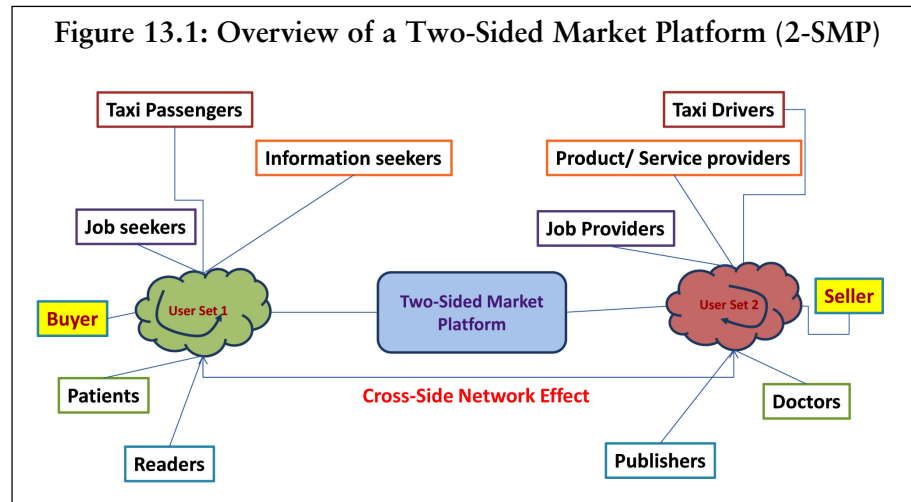
Hence, network externality is defined as the increasing utility that a user derives from consumption of a product or a service as the number of other users who consume the same product or service increases. The network effects due to these externalities can be direct or indirect fuelled by complementarity and compatibility of associated products and services.

### *Cross-side Network Effects*

The theory of Two-sided Market Platforms (2SMP) and associated platforms is not new. It has been in existence since the time Visa and MasterCard were discovered and even prior to that. In a typical 2SMP, there are two sets of users who complement each other’s usage thereby increasing the network effect for enhanced value for both. The platform enables these two heterogeneous sets of users to come together to conduct commercial transactions.

Success of the platform depends on the number of users on each side and the usage across them which is often referred to as *cross-side network effect*<sup>5</sup>. Hence, in a 2SMP, the cross-side network effects typically complement the same side network effects – direct or indirect or both. These effects are captured in the case of a typical e-commerce market place as follows. Figure 13.1 illustrates a typical 2SMP and its associated characteristics.

A typical e-market place is a platform that connects sellers of products on one side with potential buyers on the other side. The platform provides the required glue between sellers and buyers. The cross-side network effect complements the same side networks in a 2SMP as shown.



### *Pricing in 2SMP*

Pricing is one of the important strategies in a 2SMP. Typically, one set of users are subsidized while the other set pays premium depending on the price elasticity of the demand. In a two sided market with positive cross-side network effects, the platform provider, even if it is a monopolist, has an incentive to reduce platform profit. This is because in order to compete effectively on one side of the market, a platform needs to compete well on the other side. This creates a downward pressure on the prices offered to both sides compared to the case where no cross-side effects exist<sup>6</sup>.

### *Waterbed Effect*

A significant feature of the two sided market is that one group of users, choose to use only one platform, i.e. they 'single-home.' The other group, might 'multi-home.' For example, in the e-commerce platform example in Figure 13.1, typically consumers multi-home while sellers of merchandise single home. In such a market if a seller wishes to interact with consumer it has no choice but to interact with the consumer's chosen platform.

Thus platforms have monopoly power over providing access to their single-homing users for the multi-homing side. This leads to the possibility of high prices being charged to the multi-homing side. By contrast, platforms have to compete for single-homing users (i.e. sellers in the e-market place), and their high profits from the multi-homing side are to a large extent passed on to the single-homing side in the form of low prices or even zero prices. This is known as the waterbed effect and has been demonstrated in analytical models<sup>7</sup>.

### ***Competition***

The prospect of increasing returns to scale in network industries especially in 2SMP, can lead to winner-take-all battles, and hence, if not monopoly, but a relatively less number of platform providers. So an aspiring platform provider must consider whether to share its platform with rivals or fight to the death<sup>8</sup>. Coping with platform competition is a two-step process as per Eisenmann, *et al.* (2006). First, is to determine whether their networked market is destined to be served by a single platform. When this is the case, the second step is in deciding whether to compete alone or share the platform in a competition model.

### ***Taxonomy of 2SMPs***

A broad taxonomy of 2SMP is necessary to understand the scope, responsibility and liability of platform providers<sup>9</sup>.

First are e-marketplace platforms that connect buyers with sellers that normally have associated brand. These may be niche or horizontal in nature covering large number of products and associated sellers. The platforms do some due diligence in selecting the sellers. Quality of products/services is taken seriously and the platform providers do provide enough information to the buyers including ratings and facilities offered, so that buyers make informed decisions.

However, the payment for products and services are handled by the platform provider and the platform acts as a one-point contact for the customer. Moreover, these platform firms build brands through advertising and other means to attract both buyers and sellers and gain their trust. Due to the above role, these platforms normally bear limited liability and responsibility for any errors in the completion of any transaction that passes through their platforms. For example, these platform providers normally have customer grievance cell and toll free numbers for the same. They also clearly state cancellation and refund policies for the transactions done through the platform.

Second, there are essentially directory services that enable customers to get information about the products or services. These firms enable buyers and sellers to meet and complete the transactions. Though these platform providers do some due diligence to select whom to list and also provide rating services, the onus on successful partnership between buyers and sellers is normally not that of the platform provider. Given the low barriers to entry in such a service, there is often stiff competition in these types of platforms.

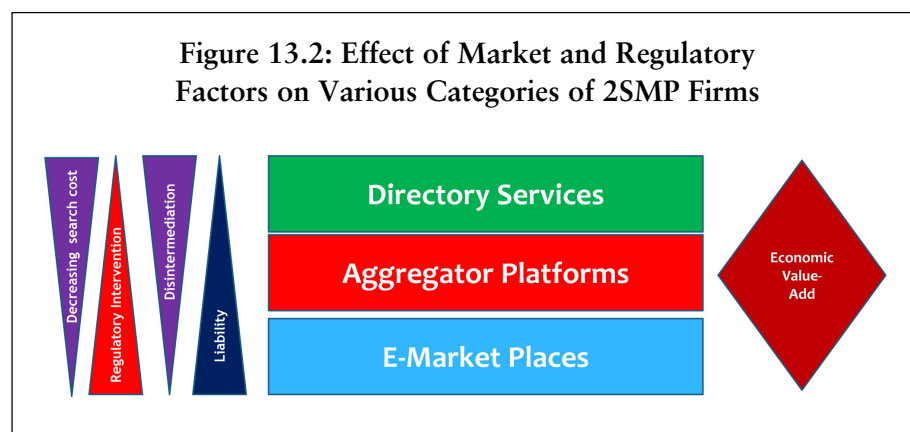


Third, are aggregator platforms who sell goods and services under their e-brand, who do not have physical counter parts, who act as one-point contact for the customer, and who source their products and services both from recognised sellers/brands as well as from individuals and aggregators who may not have any brand or even physical presence.

However, these platforms are the ones who promise to bring sanity and economic prosperity to the unorganised and informal sector workforce, especially in countries such as India. These platforms enable products and services to be made available which otherwise would not have been noticeable, and provide business opportunities for micro-entrepreneurs.

### ***Regulation and Policy***

The responsibilities and liabilities of these platforms are still evolving. Hence there is a regulatory arbitrage that the 2SMP firms try to leverage at times<sup>10</sup>. Most of the transport aggregator firms describe themselves as ‘technology platform companies’ and try to place themselves outside the ambit of regulation. Figure 13.2 illustrates how various competition and regulatory factors affect different types of 2SMP firms.



### ***Search costs***

By playing a technology based intermediation role, the 2SMP firms decrease search cost for the users on either side of their platform. In an unorganised market, search costs are often very high. Even in a relatively organised market such as in the US, the taxi sectors suffers from high search costs and Uber through its platform based approach, minimises

the search costs for both cab seekers and drivers to find each other, as pointed out by Rogers (2015).

The platform firms can potentially solve high search cost and the resultant lower supply through effective intermediation. However, the moot question is, during this process, if they bypass extant regulation, what should the policy response be? Should the extant regulation be applicable, which in effect might increase search cost and reduce associated benefits? As given in Figure 2, directory services reduce search costs more than the other forms of 2SMPs.

### ***Disintermediation***

The 2SMPs provide a way for either side users to connect with each other directly, thus reducing intermediation. In emerging countries, it is well known that intermediaries appropriate huge rents on each transaction between the two sets of users and thus reduce public benefits. Disintermediation also reduces search costs and improves the economic welfare of the two sets of users. The disintermediation is higher for directory services as they provide an easy way for the two sets of users to meet and complete their transactions.

### ***Regulatory intervention***

As indicated earlier, platforms tend to get commoditised and the winner-take-all nature of 2SMPs might lead to monopolisation or cartels in the market place. Excessive market power can threaten consumer welfare. Hence, regulatory oversight and Significant Market Power assessment is needed to avoid predatory pricing, cartelisation, and abuse of dominant power. In general the competition watchdog should frame rules that are appropriate for the 2SMPs, that is welfare enhance and does not reduce the public benefits of such market forms.

When firms in 2SMP aspire to become monopolies, they might engage in discriminate in either sets of users due to economic, political and personal reasons. There are cases in the U.S. against Uber for exhibiting such discriminatory behaviour<sup>11</sup>. What should be done against such possible discrimination?

There are also information privacy concerns due to collection of data at granular level by the e-commerce firms. While on one hand the collection and analysis of consumer data improves personalisation of services, it might invade security and privacy of individuals. What is the appropriate regulatory framework for protecting the security and privacy of individuals interacting with 2SMPs while at the same leveraging the power of technology to provide better quality of experience?

As shown in Figure 2, the 2-market places have higher regulatory arbitrage compared to director services due to nature and involvement in associated business activities.

### ***Liability***

Though firms in this space use the caveat of technology providers to reduce their liability, there are a set of minimum liability and responsibility clauses that the firms need to adhere to. For example, if one gets a spoilt food delivered by a platform provider, who should be liable? – one who delivered it (i.e. platform) or the one who produced it (i.e. the seller).

Today, most 2SMP companies provide reasonable options for returns and refunds in the case of deficient products or poor delivery service, but there are situations where the liability could and should extend beyond just a refund.

This is somewhat similar to the many cases where infringement of copyrighted material makes not only infringer culpable but even the platform that facilitated the infringement to be culpable. The answer to this question is not very obvious. However, use of the tort law to delineate between (i) intentional wrong doing and (ii) careless and negligence in causing loss financially or otherwise to the victims is essential in propounding strict or limited liability to the platform providers.

There is limited literature on the risks and associated remedies of electronic market places. Weber (2014) discusses the moral hazard problems faced by the intermediaries, especially those that provide shared accommodation and shows how all stakeholders benefit from intermediated sharing of goods. As shown in Figure 2, the liability is more with the e-market places. The aggregators also have some limited liability.

The hypothesis is that due to the above forces that shape the economic value of platforms, it can be potentially high for aggregator services compared to other two types of 2SMPs.

### **Research questions**

Based on the above, the following research questions can be formulated:

- *What are the economic models for 2SMPs for sustainable equilibrium?*
- *What are the potential economic benefits of 2SMPs?*
- *What are policy and regulatory dimensions in 2SMPs?*

This paper attempts to answer the above questions through a set of five cases in India.

## Cases of Two-Sided Market Platforms in India

In this section we analyse five 2SMPs in India, indicating their uniqueness, challenges faced, and the associated economic benefits.

### Turning yellow pages: JustDial

Though YellowPage directory services have been in existent in developed countries since 60s, in most of the emerging economies, telephone service was provided by the government or government owned Post Telegraph and Telephones (PTTs) until privatisation was initiated.

In India until 1995, the Government of India was providing telephone services through its Department of Telecommunications (DoT). The DoT used to publish Yellow Page Directory once a year and it was through this that one can get potentially telephone numbers of firms selling a product or service. There was also a government help line which was either non-functional or non-effective most of the times.

However, VSS Mani had this idea of people dialing one number and getting whatever information they needed and hence started ‘Ask Me’ service, way back in 1989. However, the service was a non-starter due to very low penetration of telephones in the country. In 1989, the tele-density in the country was 0.53 per 100 population.

Mobile services were introduced in the country in 1995 by private firms. With exponential growth of mobile phones, a decade later – in 1999, Mani launched JustDial, using telephone as a platform. JustdDial’s search service bridged the gap between the users and small businesses by helping users find relevant providers of products and services quickly, while helping businesses to market their offerings.

However, due to the ‘Receiving Party Pays’ scheme that was in existent until 2003, there was little incentive for anyone to list their names in the Directory service (Sridhar, 2012). Coinciding with the liberalisation of Internet Services in 1999, the web site JustDial.com was launched, soon to be shut down in 2001 due to the DotCom burst.

Nevertheless, JustDial was able to ride on the exponential growth of mobile services during the early 2000s along with the ‘Calling Party Pays’ scheme that was implemented by the DoT in 2003. The web site was re-launched in 2007; a decade after the domain name was registered<sup>12</sup>. The firm went public in 2013 in the country’s stock exchange.

Currently, the mobile Internet searches surpass voice/SMS searches. Finally, the mobile app revolution caught on and Just Dial released its mobile app in 2013, referred to as ‘Search Plus’ that includes listing of

any commercial product or services vendor augmented by the geo-location information.

Apart from search, Search Plus service enables commercial transactions between users and business, such as ordering flowers from local vendors, booking doctor's appointment, laundry pickups, courier pickups and grocery shopping. For example, average of 400 Doctor's appointments are booked through Search Plus; JustDial earns 2 per appointment.

About 600-1,200 food orders are placed through the platform and the platform pockets 2-10 percent of the order value as the platform access charge<sup>13</sup>. JustDial, be in its plan vanilla telephone platform based, Internet or mobile app based in a 2SMP providing director service, with information seekers on one side and commercial firms engaged in providing product/ service on the other side.

Table 13.2 illustrates the growth of JustDial and its 2SMP characteristics:

<b>Table 13.2: Growth and 2SMP Parameters: JustDial</b>	
<b>Growth Parameters (as on Mar 2015)</b>	
Number of commercial firms listed	About 275,000; mostly unorganized small businesses
Number of information seekers	15mn; addition/update of about 50,000 listings/ day
Annual searches	₹1,000mn
Revenue	₹1,562.80mn
Net Profit	₹471.60mn
Market capitalisation	More than ₹150bn
Invested firms	SAIF Partners, Sequoia Capital, Tiger Global, EGCS and SAP Ventures.
<b>2SMP Parameters</b>	
The two sides	Side-1: Information seekers; side-2: commercial firms engaged in products/ service
The platform features	Intelligent search, multi-channel (telephone, Web, mobile app), rating, direct connect between the two sets of users, sales leads
Money side	Commercial listed firms: fee range: average: ₹17,596 to maximum of ₹60,000 for premium
Subsidy side	Information seekers
Competitors	AskMe, Sulekha, ZatSe, Getit and Google (local business search), Yelp (U.S.); 58.com (China)

JustDial is a case where a platform has solved the information asymmetry problem between information seekers and small businesses. According to Eisenmann, *et al.* (2016), first mover advantage can be substantial in platform business as long as it is leveraged properly. By being the first mover in this space, and growing its listings relentlessly, JustDial has so far retained its advantage.

As per Eisenman (2006), JustDial used the product envelopment strategy to continuously provide new offerings through its platform ranging from ubiquitous voice/SMS search, web search for Internet savvy users, mobile apps for Smartphone users and combined it lately with associated services. This has kept JustDial ahead of competition.

JustDial addresses the needs of unorganised small businesses, such as local hardware shops, plumbers, mechanics, packers and movers, refrigerator and air-conditioning repair shops, which so far depended on physical foot falls and word-of-mouth recommendations for their business.

There are around 40mn small businesses in India, out of which about 500,000 have online presence. JustDial has enabled many of these small and even smaller business to come online through its platform. JustDial provided an opportunity for them to scale up their operations through its platform. This scaling up enhances the required cross side network effects and provides the glue for the information seekers and business to stick to the platform. There is potential for JustDial to scale and this will only benefit the small businesses in India to prosper.

### **Labour market revolution: Babajob**

India's unorganised work force is estimated to be around 400mn. Growth of urban centres in India has drawn a large migrant population from rural and remote parts of the country to cities. These migrant workers who are employed through middlemen do not have enough information about the labour market in their locations. Most get jobs through referrals by their community friends.

Founded in 2007 by ex-Microsoft researcher Sean Blagsvedt in the Silicon Valley of India (i.e. the city of Bangalore) with the objective of providing job opportunities for the largely organized blue collar workforce in urban areas, Babajob has come a long way. With over 1.5mn jobs and 80,000 employers, Babajob.com is India's largest informal and entry level job portal, that interconnects job seekers (i.e. employees) and job providers (e.g. employers).

Following is a quote from the founder<sup>14</sup>:

*“...I thought – if only we could digitise the job seekers and the jobs – to connect job seekers to better opportunities – we might be able to catalyse the escape from poverty for millions of people. I also looked around and saw that there were no digital tools to connect informal job seeker and employers. Thus Babajob was an idea I fell in love with, an experiment to find a scalable way to connect millions in the informal sector to better jobs...”.*

Babajob initially focussed on providing household jobs and the challenge was to attract job seekers to the platform. Started as a web portal that listed job seekers, Babajob introduced call centres for those who do not have access to the Internet. Voice/SMS services were incorporated, considering the good penetration of mobiles.

Partnership with telcos saw the implementation of ‘SMS 55444 to find your dream job’ and such campaigns followed, thus allowing Babajob to scale up to second 100,000 users. Missed call service enabled the job seekers to call a designated number, so that the call centre person could call back thus avoiding any call charges to the job seekers.

Through ties with telecom operators, the SMS subscription service was initiated with revenue sharing arrangements with Telcos. Typical job seekers include housemaids, drivers, plumbers, telecallers, receptionists, security guards, and cashiers. Apart from connecting job seekers with employees, Babajob included background verification schemes to provide authenticity of job seekers. The start-up boom in India has enabled Babajob to scale up its operations, especially for drivers of taxi aggregator companies, and sorters and delivery boys for e-commerce companies.

Babajob provides a platform for blue and grey collar jobs to seek potential employers. Platform addresses this unorganised sector and solves the information asymmetry problem between job seekers and employers in urban areas of the country. It is often very difficult to build awareness of platforms like this in the unorganised labour force.

As per Sean, Babajob went literally door-to-door advertising their services. In unorganised sector, word-of-mouth spreads faster and hence provides the required scaling up. However it is important for socio-tech start-ups like Babajob to appropriately price the money side for the platform to scale up and be sustainable.

<b>Table 13.3: Growth and 2SMP Parameters: Babajob</b>	
<b>Growth Parameters (as on Dec 2014)</b>	
Number of Job seekers listed	163,000
Number of Job providers listed	30,000
Cumulative job listings	550,000; with net monthly addition of 10,000-20,000
Job alerts sent to job seekers	1.5 Million/month
Mobile and web page views	2.5 Million/month
Markets	Large metros of Bangalore, Delhi and Mumbai
Invested firms	Grey Ghost Ventures, Khosla Impact Fund, SEEK Ltd.
<b>2SMP Parameters</b>	
The two sides	Side-1: Job seekers; side-2: employees including businesses and households
The platform features	Web portal listing of job seekers, Voice/SMS alerts, call centre, background verification
Money side	Businesses needing workers
Subsidy side	Job seekers; for Voice/SMS alerts job seekers pay charges
Competitors	Nanojobs, Merajobs, Jack On Block, Yelp (US); 58.com (China)

### **Media on local languages: DailyHunt**

Language is an important attribute of a population, and has great relevance and significance in a pluri-lingual and pluri-ethnic land like India. The total number of scheduled languages in India is 22 as per Census India 2001.

There are about 400, 100, 80, 60, and 50mn Indian population that speak Hindi, Tamil, Telugu, Gujarati and Kannada respectively. According to the 2001 Census, 30 languages are spoken by more than a million native speakers. Majority of Indians in non-metros are not comfortable in handling the English language. Unofficial estimates place the number of Indians who can speak English to be not more than 10 percent of the population. Unofficial estimates indicate that 92 percent of newspaper circulation is in local languages and there are over 700 Television channels in local language.

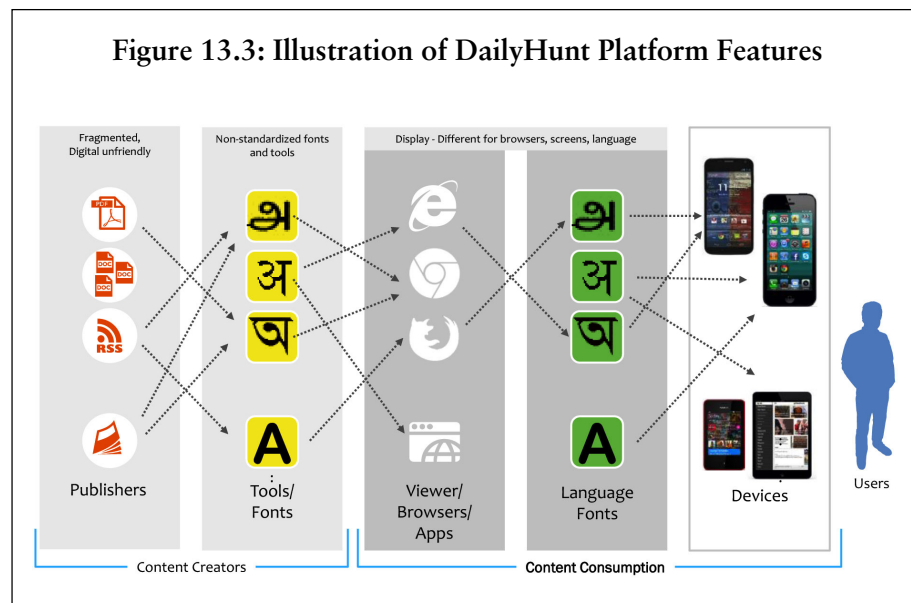
However, none of the major Indian languages figures in the top ten languages that are used in the Internet and hence about 83 percent of the users operate their phones in English, despite their discomfort. These indicate the huge need for making local language content/ app to be made



available on the Internet and through mobiles to meet the needs of this under-served market.

News aggregators are services that pull together online content in one place for ease of viewing on mobile devices. The market for news aggregator apps is dominated by Google, with its Google News & Weather for personalised news and weather content, and Google Play Newsstand for personalised curated content and topic-based collections of articles<sup>15</sup> Though there are other news aggregation services, they are all primarily for English content.

Virendra Gupta started DailyHunt (previously called as Newshunt) in 2007 with the objective of providing news in local languages on mobile devices. The Newshunt app brings regional vernacular content (both newspapers and books) from across the country to one platform. With over 36 minute installs, Newshunt is leading the digital vernacular revolution in India today. The platform connects media houses and publishers on one side with the readers on the other side. The general architecture of the DailyHunt platform is given in Figure 13.3.



The platform using its tools converts the publisher content in various languages to generic fonts and distribute to the users via web as well as app.

Apart from newspapers, DailyHunt has curated digital e-books in various languages that can be bought/ subscribed by the users for a price. The daily newspapers are available for free to app/ web users. DailyHunt claims that its users on the average spend about 184 minutes per month on and claims that it is greater than the monthly average time spent inside Flipboard (86 minutes). In July 2015, DailyHunt bought BuyT, a product discovery and recommendation platform, which would be integrated with NewsHunt for delivering product recommendations to NewsHunt users, and help it improve its mobile advertising based monetisation.

<b>Table 13.4: Growth and 2SMP Parameters: DailyHunt</b>	
<b>Growth Parameters (as on Dec 2014)</b>	
Number of publishers/ content providers	100 (25,000 articles sourced daily); 15mn local language e-Books,
Number of subscribers (readers) (i.e. number of app installs)	75mn; 20min active users
Monthly page views	1.5n
Regional languages supported	12
Invested firms	Falcon Edge Capital, Matrix Partners, Sequoia Capital and Omidyar Network
<b>2SMP Parameters</b>	
The two sides	Side-1: Content providers, publishers, and regional language writers; side-2: Content readers and subscribers
The platform features	Language support in many types of mobile devices, Publisher referrals, advertisement integration, integrated micro payment platform
Money side	Subscribers of e-Books; advertisers
Subsidy side	Readers of daily news; newspaper providers
Competitors	Google News & Weather, Google Play Newstand, Breaking News, BuzzFeed, Flipboard, Nuzzle, Vox Media, Feedly, pulse

Platforms like DailyHunt bring news and knowledge closer to the masses thus breaking the English language barrier that exists on the Internet today. By curating the content in local languages these platforms improve knowledge and awareness of citizens, thus bridging the knowledge divide.

Though China, Korea and Japan continue to produce amazing platforms that cater to the needs of local languages, the phenomenon in India is strikingly different. Unlike the one language platform in these countries, India has to cater to at least 30 language speaking population.

Hence, attaining scale economies in each language is difficult though critical. By a careful monetisation model and the fact that marginal cost of reproducing digital content is almost zero, such news and content aggregation platforms do uplift the knowledge and awareness of citizens thus creating a large consumer surplus.

### **Healthcare for everyone: Practo**

The estimated healthcare expenditure in India is about US\$150bn with a growth rate of about 12 percent, and constitutes almost 5 percent of the country's Gross Domestic Product (GDP). However, less than one percent of its GDP is government spending on public health, compared with 3 percent in China and 8.3 percent in the United States. Hence the private hospitals, clinics, diagnostic labs and doctors meet significant portion of public spending in healthcare.

Though large hospitals are relatively organised, smaller clinics, hospitals, and labs do not have an organised appointment booking, patient tracking and monitoring systems in place. Most times, patients have to wait for long hours in clinics resulting in loss of productivity.

Shashank ND & Abhinav Lal, founded Practo, a healthcare start-up in 2008. The platform on one side referred to as Practo Ray, provides automated appointment scheduling, storage of healthcare records, including x-rays, files, prescriptions and billing for clinics, hospitals and diagnostic labs. On the other side, Practo Search provides patients ways to search doctors, clinics and labs and book appointments appropriately. At the time of starting the company, the biggest challenge was to bring doctors online as the penetration of web was low and the smartphone revolution was still nascent in India.

Today, Practo claims to have nearly 200,000 healthcare practitioners, 8,000 hospitals on its platform and over 10mn monthly searches by consumers<sup>16</sup>. The growth is majorly fuelled by the focus on expansion and getting doctors on the platform. As per Shashank, "We're now looking to make Practo the Google for any information needed in the space of healthcare. Whether you need a doctor, surgeon, dentist, veterinarian or a diagnostic check-up, we will have it all at Practo"<sup>17</sup>. Practo has been using the 'product envelopment' strategy to continually augment the platform with features organically as well as through acquisitions.

The acquisitions are expected to augment Practo's platform in the areas of preventive healthcare, enterprise segment, and personalised fitness areas respectively. Currently, Practo operates in 35 cities, most of them having million plus population. The founders are also looking to expand beyond the Indian cities in to smaller towns in India as well geographies outside India that has similar needs.

The healthcare services can also be personalized using data analytics, which is one of the future areas of expansion for Practo. Currently, Practo is one of the largest doctor search platforms in Asia and is ranked sixth in the world.

<b>Table 13.5: Growth and 2SMP Parameters: Practo</b>	
<b>Growth Parameters (as on Dec 2014)</b>	
Number of Doctors/ hospitals	200,000 Doctors; 8000 hospitals & clinics
Number of	More than 1.5mn
Monthly searches by consumers	10 Million; more than 100,000 patient appointments per month
Invested firms	Sequoia Capital, Matrix Partners
<b>2SMP Parameters</b>	
The two sides	Side-1: Doctors, patients, diagnostic labs; side-2: patients
The platform features	Doctor endorsements, patient feedback
Money side	Hospitals and labs
Subsidy side	Patients
Competitors	Qikwell, Librate, HelpingDoc, Ziffi, CrediHealth

In emerging countries, large population is served by private hospitals and clinics. Without appropriate insurance coverage, the population needs a good referral system for better health care. The problem is more acute in smaller towns and rural areas. The lack of good healthcare centres in these areas force patients to go to large cities for check-ups.

However, due to lack of information and difficulty of booking appointments, the patients commute long distances and wait for their turn to see doctors. Start-ups like Practo solve this problem by providing a platform for patients and doctors to connect so that appropriate and timely appointments are made and adhered to. Digitisation of patient records and automated billing systems help doctors, small clinics and diagnostic labs in terms timely availability of accurate information about patients.

**Taxi Aggregator: Ola Cabs**

It is estimated that the radio taxi market in India is US\$6-9bn dollars growing at 17-20 percent. However, the organised market forms a very small percentage of this market. It is estimated that the number of taxis in the organised sector will reach 30,000 by 2017<sup>18</sup>.

In most of the emerging countries, due to lack of adequate public transport, a large unorganized taxi markets exist. Referred to as Radio Taxi Operators, a large number of fleet operators provide (i) airport service and (ii) inter-city service and (ii) intra-city service. These cab services are licensed by the State governments and tariff fixed by the rate card issued by the State transport department.

A native alternate to Uber came up in India in 2010, through Olacabs as an online marketplace for booking cabs and car rentals in India. The founder – Bhavish Aggarwal stated his ambition as “to change how India travels and revolutionise personal transportation in the country”.

In tune with the above, Aggarwal founded Ola Cabs disrupted this highly regulated market, by providing an easy to use platform that connected the cab renters to individual taxi drivers directly. Though Ola started its service about 3 years before Uber entered in to India, the real competition started after Uber’s entry. Started as inter-city point-to-point service, Ola started its inter-city (including to and from airport) service first in Bangalore followed by other large cities in India.

Compared to Uber, Ola customised its services to the Indian market by recruiting mini cabs, and even autos in its market place. After acquiring its competitor Taxi For Sure in 2014, Ola expanded its fleet and started providing services in 15 other cities apart from the large metros.

Using a product envelopment strategy, Ola provided driver details including photographs for identification and security of passengers, and Ola Wallet – its own payment wallet for easy payments. Ola’s market evaluation has crossed US\$1bn and has become one of the Unicorn start-ups in India. It is planning to add bus aggregation and a food and grocery delivery services as well. The other initiatives including car pooling and logistics.

Ola’s platform is very simple to use both for the passengers as well cab drivers. The passengers interact with Ola mobile app to book cabs, track, call drivers, pay using wallet, and submit review of drivers. The cab drivers are equipped with a Smartphone given by Ola that provides GPS based tracking, and billing system.

However, on December 24, 2014, an Uber cab driver sexually assaulted a woman in Delhi and was apprehended. Uber’s first claim not to take

full responsibility for the event, drew the wrath of public and governments alike against Uber and such other taxi aggregators. The taxi aggregators hired taxi drivers who held All India Permits for driving taxis.

The initial reaction from the government was that the cab aggregators are responsible for the driver who they hire in to their platform and hence should be liable for any wrong doing on the part of drivers.

From then on, it was not an easy going for Ola as there was a total ban on aggregators who were providing taxi services without the Radio Taxi Operator licence. Its operations were cancelled in many states including in the cities of Bangalore and Delhi since it was operating without the Radio Taxi license in some locations. While Ola and Uber argue that they are technology companies, not taxi operators, and come under the purview of the information technology law, government has not changed its mind.

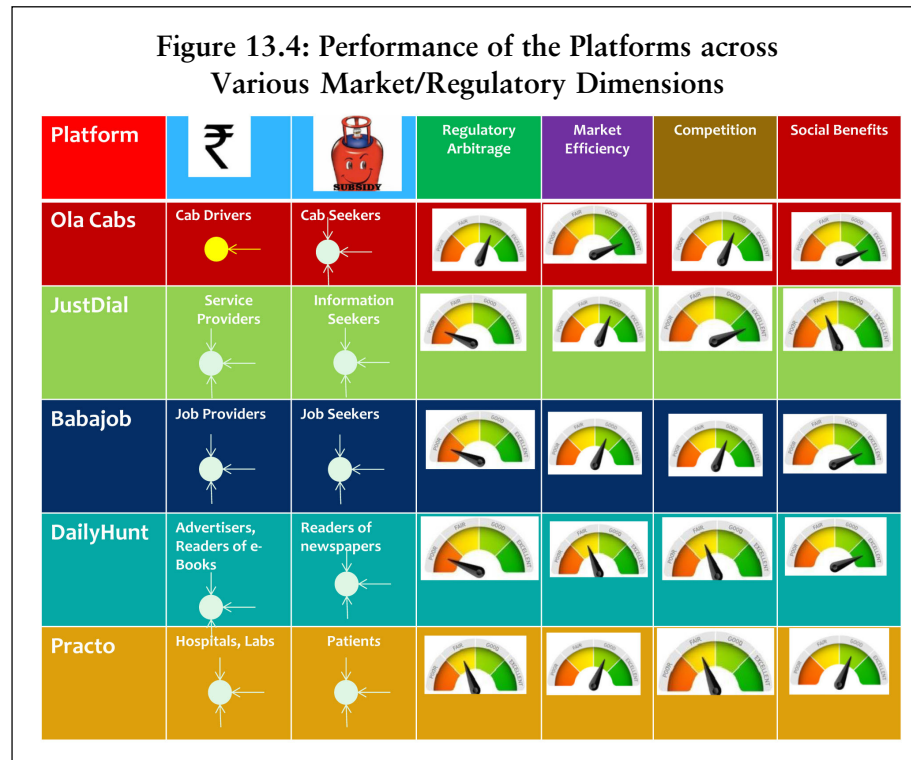
However, in a landmark judgement on July 15, 2015, the Delhi High Court suggested to the city government to do away with the ban on app-based cab service providers, saying they cannot be blamed for illegal acts of the cab drivers, who were given All India Permits (AIP) by the authorities concerned.

However, the Supreme Court reiterated that “no commercial vehicles shall ply in Delhi unless converted to Single Fuel Mode of CNG (compressed natural gas) with effect from 01.04.2001”, Justice Jayant Nath said in his order<sup>19</sup>. Hence, Ola cab is trying to convert all diesel/petrol cabs that are on its platform to migrate to CNG to continue its operations in Delhi.

<b>Table 13.6: Growth and 2SMP Parameters: Ola Cabs</b>	
<b>Growth Parameters (as on Dec 2014)</b>	
Number of taxis	2,00,000 (fleet size)
Number of cities in operation	100
Invested firms	Sequoia capital, Steadview Capital, Falcon Edge, DST Global, Matrix Partners, Softbank, Accel Partners, Helion Venture Partners
<b>2SMP Parameters</b>	
The two sides	Side-1: taxi drivers; side-2: taxi riders/passengers
The platform features	Location based taxi assignment; Passenger endorsements and feedback; automated billing; mobile wallet for payment
Money side	Taxi drivers; 15-20 percent of the bill value is paid by drivers to the platform provider as transaction fee
Subsidy side	Passengers
Competitors	Uber, Meru, Savaari, EasyCabs

### Summary of cases

Figure 13.4 gives a summary of the above five cases and indicate how they fare across different market and regulatory factors.



While social benefits are directory services, such as JustDial are minimum, they are expected to be higher for job portals such as Babajob and literary content providers, such as Dailyhunt. The market efficiency due to lower search costs and more disintermediation is higher for transport aggregators such as Olacabs. Competition effect is higher for directory services.

### Concluding Remarks and Policy Implications

As the above cases indicate, the 2SMPs in different areas seem to have generated consumer surplus, mitigated day-to-day problems of common citizens, reduced the information asymmetry problems and hence the appropriation of rents, provided better job opportunities for blue collar workers and those at the bottom of the pyramid.

Though VC funds have played their role in these platforms scaling up, the sustainability depends on the theories and outcomes of 2SMPs, including pricing strategies, stickiness of both sides of users, and the magnitude of cross side network effects.

Apart from the sustainability of these 2SMPs, the firms also have to deal with regulatory and policy dimensions that are still evolving. Countries around the world have been trying to extend the applicability of the extant laws and regulations to this platform economy. While the responsibilities and liabilities of these platforms are still evolving under the extant laws, the platforms cannot take a 'caveat emptor' approach of their legal position on their website<sup>20</sup>. Hence, the need for a balanced approach to dealing with 2SMPs and associated regulation and policies.

We indicate below certain policy guidelines for dealing with 2SMPs.

1. **Significant Market Power Assessment:** Much like in any other sector, Significant Market Power (SMP) assessment shall be done periodically by the regulator or as and when needed to prevent market dominance by one or a few set of players in the specified market space.
2. **Light touch regulation and mandatory compliance:** Since social benefits tend to be higher, the 2SMPs shall be treated with light touch regulation. A subset of existing rules shall be defined as the mandatory rules. The minimum liability and responsibility shall be defined for the mandatory compliance part of the regulation. For example, if taxi cabs need to run only on environmental friendly Liquefied Petroleum Gas (LPG), the rule should be equally applicable to those recruited by the taxi cab aggregator such as Ola Cabs. Regulatory arbitrage should not be extended in this case as the social and public harm due to highly polluting Petrol/Diesel run cabs exceed the benefits due to disintermediation and lower search costs.
3. **Fare regulation:** Though platforms tend to create larger providers, fare regulation should not be extended to 2SMPs. Since the platforms are easily replicable and there is often less barriers to entry, any predatory pricing or additional rent extraction by the incumbents will be thwarted by new entrants.
4. **Market share regulation:** Any horizontal and vertical integration shall not be discouraged by regulation. The platforms tend to attain economies of scale and scope only through integration. Due to increasing returns to scale of such platforms, integration is likely to increase social benefits. Integration also brings about the much



needed organisation to the unorganised sector, thus improving accountability, responsibility and ownership of the market place, thus providing superior benefits to both consumers and producers on the platform as pointed out by Rogers (2015).

5. Regulatory levies: Regulatory levies increase cost of providing platform service which in turn reduces the social benefits. Hence, the regulatory must be careful to avoid levying additional tax on 2SMP providers.
6. Investment regulation: The high potential of these 2SMP firms and their global characteristic have attracted foreign investments. Any restriction on ownership and Foreign Direct Investment (FDI) will affect the much needed capital for the start-ups to scale up their operations.

As has been witnessed in many cases, the incumbents often feel threatened by the 2SMP providers and lobby against them. The regulators and policy makers should be cognizant of the fact that resultant social benefits due to 2SMPs tends to be higher, and hence, not be swayed by the incumbents. Keeping a watch over the market, at the same time nurture the proliferation of the 2SMPs through light-touch regulation is the key for embracing the new technology revolution for larger social benefits.

There have also been criticisms of the 2SMPs. The simplicity of 2SMPs and hence the analytical frameworks that revolve around them were questioned in the context of Internet broadband provisioning by Sridhar & Prasad (2016). As these 2SMPs evolve in to multi-sided platforms, the economics and associated regulations have to be restructured. Further, the competition regulation also has to evolve to address the various issues including vertical integration, price discrimination and market contestability.

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## Endnotes

- 1   Rochet & Tirole, 2003
- 2   Weber, 2014
- 3   Supra note 1
- 4   Sridhar, 2012
- 5   Sridhar, 2014
- 6   Prasad & Sridhar, 2014
- 7   Economides and Tag (2012)
- 8   Eisenmann, *et al.*, 2006
- 9   Sridhar & Srikanth, 2015
- 10  Rogers, 2015
- 11  *Ibid*
- 12  Mint, 2015
- 13  Forbes, 2014
- 14  Yourstory, 2012
- 15  Kugler, 2015
- 16  Yourstory, 2015
- 17  *Ibid*
- 18  Yourstory, 2014
- 19  ET, 2015
- 20  Supra note 9

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Section IV:

# Trade, Regional Integration & Competition Reforms

Infusing competition principles and promoting regulatory reforms to make trade agreements and regional integration impactful in developing countries



# Facilitating Equitable Regional Integration through Competition Policy and Regulatory Reforms

*Key Priorities for African Developing Countries  
and LDCs in the Post-2015 Agenda*

CLAYTON HAZVINEI VHUMBUNU

*Associate Researcher, Southern African Research and Documentation Centre, Harare;  
Zimbabwe and concurrently a PhD Candidate in International Relations within the  
School of Social Sciences at the University of KwaZulu-Natal  
Durban, South Africa*

## Abstract

Many regional integration arrangements (RIAs) have adopted competition policy and regulatory frameworks to guide competition issues between and among Member States. At the multilateral trading system, the prioritisation of Competition Policy as one of the Singapore Issues at the WTO 1996 Singapore Ministerial Conference was a clear indication of the fundamental role of competition policy in regional integration and international trade. It has been generally accepted, that effective and efficient competitive and regulatory reforms at national and regional levels foster equitable regional integration considering the different levels of socio-economic development that characterise most RIAs in Africa.

Has this been the case in Africa? The grand question emerging in the face of the Post-2015 Agenda is: What are some of the key priorities in African developing countries (DCs) and least developing countries (LDCs) for effective regulation of markets for equitable regional integration and international trade? This paper establishes the critical role of competition

policy and regulatory reforms in facilitating equitable regional integration in Africa. Using a trend analysis of specific successes, challenges and prospects of regional integration in African RIAs; this paper further identifies the key Post-2015 Development Agenda priorities for DCs and LDCs in as far as competition and regulatory reforms are concerned.

The study focusses on regional integration reality cases in African RIAs, such as the Southern African Development Community (SADC), Common Market for Eastern and Southern Africa (COMESA), East African Community (EAC), Economic Community of West African States (ECOWAS), Economic Community for Central African States (ECCAS), among others.

## **Introduction**

With the intensification of regional integration and trade liberalisation, the world has been witnessing an exponentially increasing international trade in goods and services in terms of volumes and values. The World Investment Report of 2014 reveals that in the year 2013, foreign direct investment (FDI) flows to developed countries increased by nine percent to US\$566bn and to developing countries reached US\$778bn.<sup>1</sup>

On the other hand, the total global trade exports value for the year ending 2013 increased by two percent to be US\$18,8tn according to the WTO.<sup>2</sup> This signifies intensive competition for within RIAs. However, most RIAs have committed themselves to ensure equitable socio-economic development within and among Member States as part of their vision. Competition policy and regulatory frameworks are instruments and strategies adopted to guide competition issues between and among Member States. At the multilateral trading system, competition policy has been prioritised as one of the ‘Singapore Issues’ at the WTO 1996 Singapore Ministerial Conference.<sup>3</sup>

Member/Partner States in African RIAs are at varying levels of socio-economic development, and in most cases RIAs comprise one or two Member States that are far-much industrially advanced than the rest. This has largely defined FDI inflows and cross-border investment trends within RIAs.

This paper presents a critical assessment of how competition law and regulatory reforms can be adopted and implemented to achieve equitable regional integration amongst Member States in African RIAs specifically addressing the concerns of the poor citizens, producers, small and medium enterprises (SMEs), and state-owned enterprises/parastatals in small



developing countries. It will further recommend how competition and regulatory reforms can be packaged to achieve the sustainable development goals (SDGs) within the framework of Post-2015 Agenda.

## **Regional Economic Integration in Africa: Who is Benefiting?**

Since the early 20<sup>th</sup> century, regional integration schemes have been increasing through the signing of RTAs mostly by countries within the same geographical proximity. To date, RTAs are even extending beyond geography as countries seek to maximise economic, social and political cooperation within defined areas of common interest. The WTO notes that as of April 2015, a total of 612 notification of regional trade agreements (RTAs) had been received [by the GATT/WTO] and of these, 406 were in force.<sup>4</sup>

Regional integration in Africa is now driven more by socio-economic interests of Member States unlike first generation RIAs that were largely motivated by decolonisation and political unity motives. RIAs are meant to facilitate closer cross-border political, economic and social cooperation between and among Member States through progressive trade liberalisation, harmonisation of standards, regulatory frameworks and elimination of barriers to effective cooperation with the end being to foster economic growth and enhance the living standards of the citizens.<sup>5</sup> Thus out of their membership to effectively organised RIAs, it is widely argued that Member States accrue several benefits, viz, trade gains through preferential market access, reduced costs of doing business through regional trade facilitation initiatives, increased investments, regionally instigated domestic reforms, improved collective bargaining power, and returns on enhanced competition.

In economic theory and practice, the level of socio-economic benefits that RIA Member States secure from the preferential market access is largely dependent on various factors. This paper argues that national productive capacities, availability of supporting infrastructure and existence of an effectively implemented regional integration strategy at national levels are three key determinants of how many states derive reasonable gains from their RIA membership. The reality across Africa is that not many African countries can manage to maximise on these key determinants which result in more-efficient economies reaping greater benefits at the expense of less-efficient economies.<sup>6</sup>

This has been the case globally, for instance Germany and France in the European Union (EU), South Africa in the SADC, Kenya in the EAC, Nigeria in ECOWAS, Malaysia and Indonesia in the Association of South-East Asian Nations (ASEAN), and Brazil and Argentina in the Mercado Comun del Sur (MERCOSUR), among others.<sup>7</sup> Such a practical reality is always inevitable given the inherent institutional and structural differences within RIAs in terms of industrial development, hard and soft infrastructure, level of entrepreneurship, national resource and income distribution, economic governance, and among other related variables.

In Africa, this is statistically revealed by the Economic Commission for Africa which reported that in the year 2009, Nigeria and Cote d'Ivoire jointly accounted for 78 percent of intra-ECOWAS exports; South Africa accounted for 64 percent of Intra-SADC exports; Libya, Tunisia and Algeria accounted for 90 percent of intra-regional trade recorded in the Arab Maghreb Union (AMU); Cameroon provided 77 percent of intra-Central African Economic and Monetary Community (CEMAC) exports; the Democratic Republic of Congo (DRC) provided 66 percent of exports within Economic Community of the Great lakes Countries (CEPGAL) whilst Kenya accounted for 79 percent of intra-EAC exports.<sup>8</sup> Such trade domination usually depicts the existence of lopsided industrial, infrastructural and economic development within RIAs which ultimately influence the direction of FDI inflows.

The above trend, therefore, perpetuates inequitable regional integration and damaging regional disparities as liberalisation of the movement of goods, labour and capital across borders works in the economic favour of the 'big brothers' within RIAs since they are better capacitated to fully exploit the benefits of preferential regional markets and cross-border investments. As aptly observed by Lanchman, many regional integration attempts have failed because the more advanced economies were the winners of the integration and the weaker ones 'lost out'.<sup>9</sup>

It is through the use of competition law and policy that small DCs and LDCs within RIAs can develop their capacities to compete regionally and globally in the face of excessive competition whilst also ensuring that domestic industries are guarded from unfair market practices by dominant sector players.

## **Equitable Regional Development: Why Competition Policy and Regulatory Frameworks Matters?**

African RIAs have long envisioned equitable regional integration and development and this commitment is reflected in all their founding treaties. For instance, in one of the recitals in the Preamble of the SADC Treaty, Member States declared “[t]o promote the interdependence and integration of our national economies for the harmonious, balanced and equitable development of the region”.<sup>10</sup> Likewise the ECOWAS Treaty accepts “the need for a fair and equitable distribution of the benefits of co-operation among Member States.”<sup>11</sup>

As discussed and illustrated above, the reality on the ground is that few countries dominate within RIAs in Africa which obviously frustrates efforts to achieve equitable regional integration and development as envisioned. Small DCs and LDCs are struggling to survive stiff competition from firms that are expanding into their territories thanks to liberalised cross-border investment regimes.

The effects of uneven distribution of economic power within RIAs should be ameliorated by the design, formulation and effective implementation of progressive competition laws and policies in RIAs where these are not yet introduced, and the reform of competition laws, policies and regulations where these are already adopted in order to facilitate free and fair market competition so as to protect consumer welfare and further protect other players from uncompetitive conduct of their counterparts. The ASEAN Regional Guidelines on Competition Policy of 2010 defines competition policy as “government policy that promotes or maintains the level of competition in markets, and includes government measures that directly affect the behaviour of enterprises and the structure of industry and markets”.<sup>12</sup>

Competition policy and regulation seeks to ensure that the process of rivalry by companies to gain sales and make profit is not ridden by anticompetitive behaviour by firms. Regulation complements competition policy and it refers to the ‘diverse set of instruments by which governments set requirements on businesses and citizens’, and the regulations can be economic, social or administrative.<sup>13</sup>

Through regulation, governments manipulate prices, quality and quantity of goods and services with a view to achieve socio-economic sustainability whilst also protecting other players within a specific sector. It is through competition law and policy and regulation that the evils of ‘unfettered’ competition are lessened.

The increased adoption of competition policy, law and regulations by most DCs at both national and regional level is a clear indication and demonstration of its utility. Most RIAs have formulated regional competition policies and regulations, for instance, SADC has a Declaration on Regional Cooperation in Competition and Consumer Policies (2009), COMESA has the COMESA Competition Commission (CCC) and COMESA Competition Regulations, the EAC enacted the Competition Act in 2006, the Southern African Customs Union (SACU) has the Competition Agreement, the West African Economic and Monetary Union (UEMOA) has a Regional Competition and Anti-dumping Law, and the CEMAC has the CEMAC Joint Competition Regulation adopted in 1999.

As acknowledged by SADC, “[f]air competition among businesses is a cornerstone of free trade and is vital to the economic development of a region, playing an important role in promoting growth, efficiency and the alleviation of poverty”.<sup>14</sup>

Competition policy and law and regulations will thus ensure proper functioning of RIA markets and both less and more developed members of RIAs benefit from their membership. Competition policies assist in the search for equitable regional integration and development, especially considering the fact that small DCs and LDCs are more vulnerable to abuse of market power by firms through engaging in anticompetitive behaviour, such as abuse of monopolies, monopsony, market-distorting subsidies, bid-rigging, collusions, cartels, abuse of dominance or market power, price fixing, anticompetitive mergers and acquisitions, predatory pricing and dumping, and exclusionary practices, among others.

It has been widely argued that the effective implementation of competition policies at national and regional levels within RIAs has the massive potential to reduce the exercise of anticompetitive behaviour and then spur competition which promotes competitiveness and innovativeness; gives incentives to firms to improve their allocative and productive efficiency which reduces market prices of goods and services thereby enhance consumer welfare.<sup>15</sup>

One of the main reasons why small DCs and LDCs are being left behind in regional socio-economic development within RIAs is that the socio-economic disparities within RIA economies is not well-regulated to the extent that small DCs and LDCs are struggling to cope and compete. Due to regional trade liberalisation and reduced barriers to entry, small firms or SMEs would need strategic protection and a level playing field in the face of more efficient regional or cross-border investments.

With reference to the EAC, Mutabigwa argues that competition law in the East African regional body will ‘help protect SMEs from the vagaries and greed of larger companies in the region’ whilst assisting to ‘unlock potential for SMEs to blossom and in the process benefit EAC consumers.’<sup>16</sup>

Within COMESA, cartels have been reported in the fertiliser, bread and construction industries.<sup>17</sup> And as noted by the United Nations Conference on Trade and Development (UNCTAD), whilst cartels have adverse effects on all consumers, it is the poor citizens and SMEs who suffer more.<sup>18</sup> In a recent study by Ivaldi et al (2014) focussing on 38 countries in Africa, Asia, Latin America and Europe; it was confirmed that ‘cartels impact in developing countries can indeed be substantial.’<sup>19</sup> Cartels are formed when competing firms (producers or manufacturers) tacitly collude and agree to fix prices, market shares and allocate customers with a view to reduce competition and increase profits.

The above is also the case with firms that engage in vertical and horizontal collusions, predatory pricing or abuse of dominance. In most instances, such companies engaging in anticompetitive behaviour are usually created out of FDI inflows in small DCs and LDCs. FDI in RIAs is mostly concentrated in more advanced economies. With time, these companies expand into other RIA Member States through cross-border investments. As observed by Levenstein and Suslow (2004), cartels [and other large firms likely to abuse their market dominance] usually form industrialised countries and this has ‘simultaneously harmful effects on developing producers.’<sup>20</sup>

The fatal effects on DCs can even be worse when it comes to hard-core cartels formed by very large competing firms.<sup>21</sup> This will force SMEs out of the market whilst at the same time making it difficult for new investments to enter the market yet the key objective of RIAs is trade and investment liberalisation. The suffocation of small firms is detrimental to socio-economic development of small DCs and LDCs given that SMEs are ‘necessary engines for achieving national development goals such as economic growth, poverty alleviation, democratisation and economic participation, employment creation, strengthening industrial base and local production structure.’<sup>22</sup>

When SMEs are driven out of the market due to anticompetitive practices of large firms, the end result is inequitable regional integration and development whereby small DCs and LDCs in RIAs experience stunted industrialisation, slow economic growth and minimal employment creation whilst the more industrialised economies, within the same RIA, progressively experience more socio-economic development.

Across all African RIAs, anticompetitive practices has always been to the advantage of regional giants. The merger case of East African and South African Breweries was argued to have an immediate effect of lessening competition in EAC, with small DCs and LDCs in EAC such as Rwanda, Uganda and Burundi likely to feel the impact more.<sup>23</sup> Similarly in EAC, concerns have been raised over allegations of anticompetitive behaviour by Safaricom, SABMiller, Kenya Breweries, Tanzania Breweries and MultiChoice Kenya's DStv brand.<sup>24</sup>

In SADC, South African-owned companies are dominant throughout the region and beyond. Given their huge capital base, production efficiency and technological advantage, they can easily out-compete small firms within the RIA. Effective competition policy and regulation is key to ensure that these firms compete with domestic firms fairly. For instance, South African Breweries (SABMiller) operates in 15 African countries within SADC, COMESA and ECOWAS, over and above operations in Europe, North America, and Asia Pacific.<sup>25</sup>

South Africa also has several firms investing in mining, manufacturing, transport, energy, food processing, financial, telecommunications, retailing and tourism sectors within SADC and beyond. By April 2015, Shoprite (a retail joint), had 357 outlets in different African countries, including 115 Shoprite supermarkets, and more than 100 other furniture, home decor, pharmacy and restaurant stores in 14 African countries.<sup>26</sup>

In EAC, Kenyan firms dominate the region. By 2012, Kenya was reported to be the biggest EAC investor in Rwanda with firms investing in the banking sector (namely Kenya Commercial Bank, Equity Bank, I&M Commercial Bank, and Fina Bank), retail stores, and education.<sup>27</sup> The case has also been the same in ECOWAS wherein Nigerian firms such as Dangote Cement, Dangote Sugar Refinery, Guaranty Trust Bank Plc, Zenith Bank PLC, and Stanbic IBTC Bank, among others, were singled out as grabbing a huge market share within the regional block.<sup>28</sup>

Given the companies' huge capital base, as evidenced by Dangote Cement with a market capitalisation of US\$10.5bn, the ramifications of their operations in small countries will be fatal if left unregulated since these big firms take advantage of their strength and maximise on economies of scale which the small domestic players cannot manage.

The significance of competition policy and law in this regard can never be under-estimated if equitable regional integration and development in African RIAs is forever to be attained. Most large firms take advantage of national competition authorities with weak capacity to investigate and prosecute anticompetitive practices coupled with absence of effective regional competition law and policy institutions.

## **Assessing the Implementation Record of African Regional Competition Instruments**

As argued earlier on, developing regional competition laws and policies is crucial in assisting RIAs to adopt a comprehensive regional approach when dealing with anticompetitive behaviour exhibited by foreign companies whilst facilitating regional cooperation on matters of competition whenever RIAs engage or negotiate with others players in the multilateral trading system. This ensures that RIAs accrue the benefits of regulated competition and sustains competitive market interaction within the region. However, RIAs are making varying progress in adopting regional competition regimes and have been experiencing several challenges in the processes.

Some RIAs are yet to establish competition authorities/commissions/bodies to enforce competition laws at the regional level and harmonise Member States' national competition regimes. The absence of regional regulators definitely perpetuates rampant cross-border anticompetitive practices by firms which heavily affects weaker market players and also encumbers the operation of a fair trade market system within the region. COMESA has already established its Competition Commission. The EAC has made commendable progress, albeit at a slow pace, in establishing its own regional competition authority.

In October 2015, the setting up of the EAC Competition Authority which had been set for July 2015 was reported to be delayed by the Partner States of Burundi, Rwanda and Uganda which were yet to submit their nominees for commissioners to sit in the board.<sup>29</sup> This is against a background where the EAC Competition Act was enacted in 2006, but it is almost a decade before the RIA sets up a regional competition body.<sup>30</sup> At least the EAC Competition Authority is now scheduled to begin work in the year 2016.<sup>31</sup>

Other RIAs such as ECOWAS, SADC and AMU, among others have made progress in adopting competition regulations and declarations but are yet to establish regional competition authorities. This challenge has been compounded by the absence of competition regimes within Member States themselves. For instance, although Tanzania (with Fair Competition Commission for Tanzania) and Kenya (with Monopolies and Prices Commission for Kenya) have the most advanced competition laws and competition authorities within EAC, Burundi and Uganda are yet to enact national competition legislations.<sup>32</sup>

Certainly, this does not only slow down the process of adopting competition regimes at regional levels, but also result in implementation complexities and inertia whenever the regional competition laws and policies are finally adopted.

Where regional competition laws and authorities exist, there is very little awareness on their existence and importance by the stakeholders. As argued by Odhiambo, the slow progress in the implementation of EAC Competition Act of 2006 is as a result of this factor.<sup>33</sup> The recommendation is that there should be more awareness, training campaigns and sensitisation programmes in RIAs to ensure effective implementation of regional and national competition law and policy and regulations (CLPRs). Trade Mark Southern Africa (TMSA) says “media coverage could help to promote a culture of competition by increasing awareness among consumers and other stakeholders”.<sup>34</sup> COMESA is already implementing this strategy. In July 2015, the CCC organised a sensitisation workshop in Livingstone, Zambia for business journalists to raise awareness in the region through media reporting.<sup>35</sup>

Competition authorities in RIAs are facing the challenges of conflict of jurisdictions. Whilst national competition laws principally apply to transactions that affects one Member State, and regional CLPRs apply to transactions that have a regional impact or cross-border dimension; there have been challenges of uncertainty in cases that some transactions found themselves being referred to either of the two. For instance, the CCC even acknowledges that in some instances “Member State(s) requests for a referral of the transaction to be assessed that Member State’s national law as provided for under the Regulations.”<sup>36</sup>

In any case, the reality is that given the global nature of business in contemporary times, it is now difficult to find business transactions whose impact can be exclusively confined within national borders whilst even business transactions that are considered to have a regional dimension also have a national perspective.

In the case of EAC, TMSA observes that there are “legislative conflicts between national and EAC competition regimes leading to disharmony and enforcement hurdles”.<sup>37</sup> Moreover, some regional competition laws are defective and laden with legal loopholes. For instance, some regional completion legislations contain provisions that do not have regulations to that effect. This is the case with EAC Competition Act of 2006 which has provisions on subsidies but does not have regulations to this area.<sup>38</sup> This, therefore, calls for amendments to regional competition laws to ensure that they are aligned.



However, such a process should be initiated first at the national level where in most of the countries' cooperation between competition authorities and sector regulators is blurred and conflictual. It is the urgent address of such institutional challenges which is key in search of regional harmony. Horizontal collaboration (between and among RIA competition authorities), and vertical collaboration (between RIA competition authorities and national competition authorities at national level) can prove helpful in this regard. This is key for information exchange, joint investigations, capacity building and sharing of best practices.

For instance, CCC signed a Memorandum of Understanding (MoU) with the Competition and Fair Trade Commission (CFTC) of Malawi on September 04, 2015 which seeks to facilitate and promote the harmonisation of competition laws of the CCC and CFTC as well as foster cooperation in capacity building programmes, exchange of information on investigation and consultations.<sup>39</sup>

Overlapping membership to RIAs poses a challenge in the smooth implementation and enforcement of regional competition laws and regulations as it may create inter-RIA conflicts of jurisdictional nature. With the African regional integration spaghetti bowl reality, wherein countries such as the Democratic Republic of Congo (DRC) belonging to several RIAs, namely COMESA, SADC and ECCAS, the policy conflict dilemma is an inevitable implication. Likewise, when it comes to the domestication and implementation of competition policy regimes, complications arise.

Initiatives such as the COMESA-EAC-SADC Tripartite Free Trade Area (TFTA), and the African Continental Free Trade Area (CFTA) both launched in June 2015, are recommended. The TFTA has worked on the establishment of a harmonised Joint Competition Authority which will assist in curing effects of the regional jurisdictional overlap and conflict in competition rules within overlapping RIAs. It is refreshing to note that the TFTA Joint Competition Authority on Air Transport is now in place.

The mere fact that RIA member states are at different levels of economic development is an impediment to the effective implementation of competition laws. This has been the case in RIAs in developing countries within which there are apparent economic development disparities. Using the case of EAC, TMSA argues that this scenario results in 'a quest for protectionism by the governments of some of the EAC member states'. This is made worse by the fact that transaction fees remain very high. Smaller economies, which are usually dominated by relatively smaller firms, are severely affected than their more economically advanced counterparts.

For instance, in COMESA, merger notification filing fees cap is pegged at US\$200,000, itself a reduction from the US\$500,000 set until 2014. This affects business operators.

There are also challenges related to the independent status of competition authorities at regional and national level. Since most competition authorities are hardly independent from the state, as they are politically and administratively subordinated to the government; they are easily manipulated to protect the interests of a political elite and small/powerful minority business players. Moreover, they get their budgets come from the state. This is the case with almost all national competition authorities in SADC member states. As a result, there is a tendency that anticompetitive behaviour by government bodies or parastatals are rarely investigated in an impartial manner. This distorts the regional market in RIAs.

## **Key Priorities for Africa in the Post-2015 Agenda**

Regional integration, as stated above, ultimately aims at enhancing the equitable and sustainable socio-economic development of Member States. The United Nations Development Programme (UNDP) notes that regional integration ‘holds considerable promise for supporting inclusive growth and accelerating and sustaining human development outcomes’ and further points out that ‘human development considerations’ should be incorporated from the onset in order to achieve results.<sup>40</sup>

With the intensification of cross-border investments and trade in goods and services within RIAs, it is critical for African countries to focus on collectively pursuing the SDGs through ensuring that their competition law and policy and regulatory frameworks address the issue of equity and inclusivity in development.

In pursuit of the SDG number 10 which aims to ‘reduce inequality within and among countries’, African countries have the obligation to reform their national and regional competition law and policy and regulations such that they promote industrial competitiveness, eliminate anticompetitive behaviour and promote fair competition, enhance productive efficiencies, promote the growth and expansion of SMEs through technology transfer and progressive partnerships which ultimately promote sustainable and inclusive growth across all African RIAs.

Thus, in the Post-2015 Development Agenda, the key priorities for DCs and LDCs in African RIAs should be to fully develop and adopt regional competition law and policies; align national CLPRs with regional

competition law and competition policies; develop effective regional implementation mechanisms to ensure compliance.

Whilst most RIAs such as COMESA, EAC, SADC, SACU, UEMOA, CEMAC, ECOWAS, among others, have made noticeable strides in developing competition law and policy and regulatory frameworks, the success of these regional competition policies is dependent on the existence of effective institutional and legal enforcement mechanisms. It is through an effectively implemented regional competition policy framework that the differences in terms of industrial development and the apparent economic disparities existing within African RIAs are not worsened.

DCs and LDCs, through their collective efforts within RIAs, should prioritise addressing the above-explained challenges and ensure effective regional competition policy implementation, it is imperative that the competition law is well-designed and the institutional framework to administer the competition law and policy is capacitated enough to carry-out its functions in terms of human, technical and financial resources as well as conferred with the necessary powers to execute its functions. Capacity building of both regional and national competition authorities is critical.

Regional competition laws should be structured with clear guidelines on how national and regional competition authorities interface in a complementary and harmonious manner so as to avoid conflicts over the scope of their respective jurisdictional enforcement powers. The extent of application of the principle of subsidiarity in RIAs should be considered.

RIAs in DCs and LDCs also need to prioritise the harmonisation and amendment of both national and regional competition laws so that they are aligned to each other. Further, competition law enforcement can only be strengthened by introducing a stronger and more effective RIA community law system that allows for more powerful regional court system. For instance, COMESA has the COMESA Court of Justice (CCJ) for the re-dress of competition law and empowers COMESA citizens to take even their governments to the CCJ for competition law-related cases. Complementary initiatives will also be helpful to strengthen the implementation of regional competition laws and policy in RIAs.

For instance, COMESA established a 'One-Stop Shop' so that 'all transactions with an appreciable effect on trade between Member States are filed with the CCC instead of having these filed with individual Member States'. The 'One-Stop Shop' concept ensures regional fluency in dealing with competition issues within RIAs.

With properly regulated markets and fair competition, the African regional integration process will be more even and equitable thereby ensuring inclusivity and sustainability in regional development. It is inevitable that small DCs and LDCs, and the more advanced members of African RIAs usually have divergent economic interests as the former are more inclined to be over-regulative and protective of their markets and domestic industry, whilst the latter exhibit tendencies of being over-protective of RIA markets and at the same time pressure less economically advanced RIA member states to liberalise markets through de-regulation and relaxation of competition constraints. Political will and commitment from both sides is needed in order to strike ‘win-win’ outcomes.

## **Conclusion**

African RIAs have intensified regional trade and cross-border investments through progressive trade liberalisation. More advanced economies within RIAs have taken advantage of trade openness to venture into regional markets thereby establishing market dominance leveraging on scale economies. There is a propensity to engage in anticompetitive business practices by larger firms investing from more advanced economies through forming cartels, price fixing, bid-rigging, collusions, abuse of dominance or market power, anticompetitive mergers and acquisitions, predatory pricing, among other practices. Such practices perpetuate inequitable development amongst RIA members.

African countries should address the legal, policy, structural and operational challenges that they are facing at national and RIA level with regard to the implementation of competition laws and policies so as to ensure equitable regional integration. Only reformed and capacitated competition law and policies can assist in restoring fair competition within RIAs. The full adoption of regional competition law and policies, together with the establishment of effective enforcement mechanisms is considered key in pursuit of the post-2015 Development Agenda, specifically the achievement of SDG number 10 which aims ‘to reduce inequality within and among countries’.

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# Broadening the Discourse on Regional Trade Agreements and Competition Rules, Compliance and Performance in Developing Economies

DEREK IRELAND

*Arthur Kroeger College Fellow  
Carleton University and  
Economic Consultant  
Ottawa, Canada*

## Abstract

The purpose of this paper is to broaden the current discourse on regional trade agreements (RTAs), market integration, and the competition rules and obligations within RTAs. The paper describes some of the major issues, practical lessons and ‘best practices’ on how competition policy and law and related regulatory reform obligations within RTAs that have developing economy and other lower income member states, can promote regional integration, more inclusive economic growth, improved livelihoods, and sustainable development across member states. The paper draws on the experience, successes, and challenges from incorporating competition policy and law and related regulatory reform obligations within many RTAs over the past 30 years. Because of the Conference’s location in Nairobi Kenya and the author’s recent consulting experience and research, special attention is given to the efforts of COMESA, SADC and other African regional trade agreements to promote competition and



related regulatory reforms in their regions and member states, which in some cases have overlapping memberships.

The paper has two main arguments. The first argument is that competition and related regulatory reform initiatives and obligations can strengthen economic growth and regional market integration within RTA regions that have developing economy members; and can also promote stronger competition regimes, including improved compliance with and enforcement of competition and related policies, laws and regulations within and between the region's member states. The second argument is that developing economies have available to them a variety of regional competition models, which offer their own distinct benefits, opportunities and challenges. Two arguments and major issues are assessed in this paper through employing a more comprehensive and hopefully innovative methodology, which incorporates to some degree the insights from behavioral economics, neuroscience and other less conventional literatures.

## **Introduction and Background**

Developing economies presently have available to them a rich literature and practical real-world experience on incorporating competition rules and related regulatory reform obligations into their regional trade agreements. This paper will largely focus on competition rules and obligations within RTAs, but many of these issues are also relevant to related regulatory reform commitments. The major findings in this paper are based on an extensive review of the RTA literature of the past quarter century and the author's personal experience over the same period in government and the private sector, including:

- Conducting in 2011 an EU project to assist the SADC Secretariat and the region's 15 MS to enhance the design and effectiveness of competition, consumer and related policies, laws, regulations and SADC's information sharing and enforcement cooperation initiatives and platforms.
- Canadian representative and active contributor to OECD and related Canadian work in the first half of the 1990s on competition policy and law convergence and enforcement cooperation, the competition law challenges faced by transition and developing economies, and the interactions between trade and competition policies.

- Consulting work on urban and regional development and infrastructure planning in China and other Asian developing economies over a 15 year period, which focussed on regulatory reform and the introduction of competition in previously regulated infrastructure and other sectors.
- PhD research programme and dissertation from 2003 to 2008 on competition policy, law and institutions and regulatory reform in developing economies, the evolution of competition policy and law in India from 1965 to 2008, and the implications for India's traditional business groups, other businesses and its new competition law.
- Personal research, published articles, conference presentations, and consulting assignments for the Government of Canada on competition and consumer policy and law, and regulatory reform, modernisation and impact analysis – including the consumer benefits, costs and risks and related competition, supply-chain and business impacts from domestic regulatory reform, and enhanced regulatory alignment and cooperation between Canada and the United States under the Regulatory Cooperation Council agreement of 2011.

Section two of this paper describes the potential regional and competition benefits from incorporating competition rules and obligations in RTAs. Section three summarises some of the lessons on MS differences to be accommodated, and the RTA approaches that can be problematic for competition and market integration. Section four lists some of the major questions to be addressed when determining the preferred RTA competition model, and the final section returns to the two major arguments presented in the Abstract and provides suggestion on future ex-post research. Appendix A provides an overview of competition policy and law obligations and progress in selected regional trade agreements.

## **Potential Regional and Competition Benefits from Incorporating Competition Obligations in RTAs**

### **Benefits to Regional Trade Agreements**

Much of the trade and competition literature on competition and related barriers to trade has focused on the benefits to RTAs and their member states from incorporating competition policies, rules, institutions

and obligations within the RTA framework. These include the ability of regional competition laws, rules and agreements to address and remedy:

- government and private barriers to business entry, establishment and growth and related anticompetitive conduct and arrangements and barriers to market access within national borders, which cannot be reduced by lower tariffs and quotas and other trade policies and instruments;
- cross-border anti-competitive practices of private and public enterprises that harm two or more MS, act as trade barriers, and could not be remedied by trade policies;
- potential negative interactions between competition and trade liberalisation when more open MS and regional markets can lead to the ‘importation’ of cartels, abuse of dominance, and other anticompetitive business practices from other members and from businesses and governments outside the region; and,
- the anti-competitive effects of trade remedy laws, through employing competition rules rather than anti-dumping, subsidy and countervail, safeguards and other trade policy instruments.

## **Benefits to Competition Authorities and Regimes**

Less attention in this literature has been given to how embedding competition rules either formally or informally within RTAs can provide important benefits to the competition policies, laws, and authorities of members. The RTA and its major objectives, provisions and obligations on trade, investment, technology, industrial policy, and related regulatory reform and marketplace issues can inform and guide member state competition laws, policies, and institutions, and can ‘frame’ domestic discourse on competition policy and law in a more positive manner that:

1. Promotes and accelerates the introduction of new and better national competition policies, laws, and authorities – that are more likely to survive new governments that have different views about the importance of fair competition to socio-economic development and prosperity.

And that, through positive encouragement, technical assistance, and the threat of ‘naming and shaming’, accelerates the introduction of modern competition laws and authorities by the MS sceptics and laggards that otherwise might delay the introduction of modern competition laws and authorities for years and even decades.

Expands the visibility, credibility, legitimacy, independence and effectiveness of the competition authorities and regimes in each MS through:

- promoting formal and informal convergence, alignment and cooperation between members
- strengthening the competition compliance cultures within MS
- reinforcing and disciplining concurrent competition and related regimes such as sectoral regulators, fair trading laws, and foreign investment rules
- increasing the potential for competition rules to take precedence when there are conflicts with sector specific and other regulations, and with trade, industrial, innovation, intellectual property, and other policies
- reducing political, bureaucratic and vested interest influences on competition law enforcement – including from powerful and entrenched business groups and conglomerates and
- more readily identifying the competition regime ‘slackers’ that are not meeting their RTA obligations through failing to establish a modern competition regime, or through weak, incorrect, and/or politically influenced enforcement of their existing national competition rules.

The trade and competition literature, combined with recent advances in the behavioral, neuroscience, institutional and related literatures, indicate that MS and regional efforts to better align policies, laws, regulations, analytical methods, and compliance, enforcement and education functions – and increase information sharing and enforcement cooperation between national authorities – can reduce the administration and compliance costs, irritants, frustrations, as well as the excuses and rationalisations to not comply, of companies, industries and other regulated entities.

As a consequence of these and other institutional, behavioural and social mechanisms, enhanced alignment and the establishment of cooperation platforms promote competition rules compliance and performance through improving relationships between the authorities and the regulated population, and making compliance easier, less costly, more automatic, and the ‘default option’ for companies and other regulated entities.

2. Allows member state authorities within RTAs, with regional competition authorities that have case enforcement responsibilities

and capabilities, to transfer more economically complex and politically sensitive and divisive merger, cartel, abuse of dominance and other enforcement cases to the regional authority.

Thereby helping to preserve the effectiveness and credibility of competition policy and law throughout the region. Moreover, member states can apply the RTA rules domestically until national competition laws and rules are in place.

3. Provides regional technical assistance, expertise and support that make it easier for member states to establish new or more modern competition laws and authorities. The experience of South African Development Community (SADC) and other RTAs indicate that support and assistance from the competition law MS leaders and the regional authorities in both more formal and informal RTA regimes can be especially helpful to the establishment of functioning competition laws and authorities in smaller member states. Evidence on the importance of regional assistance and support has been provided by both more formal and informal RTA models, but as noted in point three above can be, especially important for RTA competition regimes with regional authorities that have enforcement responsibilities and capabilities.

Furthermore, being a member of an RTA strengthens the arguments for smaller and less developed economies to establish their own competition policies and laws because of the risk of ‘importing’ cartels and other anticompetitive conduct, arrangements and harms when trade, investment and other barriers are reduced under the regional trade agreement (see above).

4. Broadens political, bureaucratic, business, consumer, public and voter interest, understanding and support for competition policies, laws and authorities.

Through clearly establishing the linkages and causal relationships between RTA and MS competition rules and obligations, and the RTA’s broader trade, economic development, industrial policy, inclusive growth, equity, sustainable development, and other economic and social objectives that are more understandable to many stakeholders and the general public.

Great support would be expected to expand through time by means of the growth in trade, investment and technology flows between MS, and a growing regional business community and other stakeholders that are benefitting from the RTA and its competition

rules. Making these linkages and causal relationships clearer can, especially build support for competition policy and law among the key ministries responsible for finance, international trade and investment, and industrial, innovation and economic development.

5. Facilitates the more rapid establishment and more effective deployment of bilateral and multilateral information sharing, positive and negative comity, and enforcement cooperation agreements and platforms between members and with countries outside the RTA.
6. Encourages the application of more dynamic and forward looking analytical frameworks for mergers, Abuse of Dominance (AOD) and other rule of reason cases – through taking account of the RTA’s current and future progress and achievements, and the remaining constraints to regional market integration that can be addressed through competition advocacy and compliance promotion programmes.
7. Reduces the number and complexity of enforcement cases of in particular under-resourced and less experienced Member State Competition Authorities (MSCAs) – through regional integration, more open borders, lower trade and entry barriers, and regional information sharing and case enforcement cooperation involving more experienced competition authorities (CAs).
8. Brings regional presence and bargaining leverage to competition matters and enforcement cases that involve large international corporations; and sends a strong message to regional and external businesses that there is “no place to hide” when they attempt to establish cartels and other anticompetitive arrangements within the region.
9. Provides opportunities for developing economy and other MS to more efficiently and effectively participate in and benefit from global competition policy and law and related policy networks – Industry Capability Network (ICN), Organisation for Economic Cooperation and Development (OECD), United Nations Conference on Trade and Development (UNCTAD), World Trade Organisation (WTO) etc. and the regional networks now emerging in Africa, Asia and Latin America.

And therefore allows developing economy member state (MS) to compete on a more equal footing in the ‘market for competition policy and law ideas’ that is now dominated by the United States and the European Union.

10. Can generate positive externality, feedback and demonstration effects within other regulatory regimes of the RTA and its member states – when regional competition successes encourage the establishment of regional cooperation platforms in other policy and regulatory areas.
11. Potentially can provide competition, consumer and/or trade benefits to neighbouring and other non-members, which can help to offset any actual and perceived trade distortion and diversion effects of the Regional Trade Agreements (RTA).

Through these and other positive outcomes, incorporating competition policies, laws, and rules within RTAs can increase stakeholder interest in, understanding of, and support for the regional and MS competition regimes, and pressures for competition regime improvements – which go beyond the traditional competition policy and law community.

Future ex-post research should focus on the dynamic, interactive, cumulative, lock-in, feedback and related path dependent effects between the support that competition policies, laws, rules and institutions receive from being incorporated within RTAs, and the broader benefits that RTAs receive from these competition rules and obligations (see section 5.0 below).

## **Contributions from More and Less Formal RTA Models**

The literature and authors’ experience suggest that these RTA benefits from ‘embedded’ competition obligations can be generated by either EU type formal models or more informal, ‘best efforts’ models of North America Free Trade Agreement (NAFTA), South African Development Community (SADC) and Association of South East Asian Nations (ASEAN). Future ex-post research should explore whether and the extent to which, for some RTAs, the more informal models with lower negotiation and implementation costs could generate net benefits that are comparable to or greater than the EU type models.

For example, the number of SADC MS with functioning competition laws has expanded from three in 2004 to eleven in 2015; ASEAN and

APEC have been making similar progress in recent years; and Mexico reportedly accelerated the introduction of its modern competition regime when this became a NAFTA obligation. Informal commitments, moral obligations, aspirational objectives, policy entrepreneurs within member states, and ‘modernisation’ to keep up with the competition Joneses”, can be major drivers of change in some national and regional settings.

Moreover, the behavioral, psychological, neuro-economics, institutional and other less conventional literatures illustrate that, under some circumstances, MS incentives and motivations to comply with informal and best efforts commitments can be equal to and even greater than more formal regimes that employ binding commitments. Furthermore, MSCAs under these regimes can be just as willing to impose monetary, reputational/naming and shaming, social and other penalties on non-complying and uncooperative members.

## **Problems and Challenges Associated With RTA Competition Obligations**

### **MS Differences to be Accommodated**

Many articles on RTA competition rules that involve developing economies have focused on the constraints, mistakes, and alleged failures of regional rules and authorities. This author prefers a more positive ‘glass-is-half-full’ approach, in order to identify progress, lessons, best practices, and challenges that can be addressed and remedied through time. The RTA competition literature indicates a number of conditions that can raise challenges but do not prevent formal and informal regional competition rules from generating benefits for the RTA region and its member states and stakeholders. Reasonable benefits can occur even when:

- Members are not at the same or similar levels of economic, social, political, and institutional development; and MS competition regimes are not at the same or similar levels of development and experience.
- Not all MS have modern competition laws, rules and authorities from the outset – although this should be the long-term goal except for the smallest “microstates” in e.g. CARICOM and other RTAs (see Appendix A).
- Full agreement and consensus have not yet been achieved on more general competition policy and law principles, standards, coverage



and interventions, such as using competition rules to discipline government subsidies, procurement practices, and state-owned enterprises, and to replace antidumping, countervail, safeguards and other trade remedy laws. At the same time, the EU model and Closer Economic Relations (CER) agreement clearly indicate that replacing anti-dumping with competition rules is feasible and beneficial given the required political will and some commonality in the relevant competition rules and their enforcement across member states.

- As long as there is some common ground on core principles, objectives, the anticompetitive conduct to be addressed, and analytical methods, some diversity in objectives, standards, enforcement practices, coverage, and cultures can be accommodated; and can promote experimentation, innovation, and imitation and learning from more experienced MS jurisdictions. Based on the SADC experience, developing common ground can be facilitated by: “organic convergence” across MS in competition rules, case selection, analysis, and management, market definition, and enforcement methods; and the preparation and distribution of practical “best-practice” guidance documents on key enforcement and analytical issues and enforcement cooperation platforms – which led to the launching of SADC’s web-based competition case resource database in 2012.

For similar reasons, not all RTAs in the global economy need to adopt the same regional competition rules model. Some experimentation, innovation and healthy global competition in the design and administration of RTA competition rules are desirable.

## **RTA Approaches That Can Be Problematic for Competition and Market Integration**

RTA scholars and competition law practitioners have also identified some aspects of region-wide competition rules and their enforcement that can be problematic for competition and market integration under RTAs.

Their research indicates that only competition penalties should be applied to anticompetitive conduct and arrangements in the RTA and its MS. Applying trade sanctions to the member states where the anti-competitive conduct is taking place can have more negative effects on

competition, consumer welfare, efficiency, market integration and other public welfare objectives than the anticompetitive conduct that is being sanctioned.

Evaluations and assessments of existing RTAs with regional enforcement functions also suggest that competition and market integration problems can arise when:

- (i) The RCA does not have the mandate to conduct its own cases and apply its own competition penalties, without first receiving approval from the affected member states.
- (ii) Trade effects tests for allocating enforcement and other matters to the RCA are interpreted in a very narrow manner that limits the regional investigation and sanctioning of anticompetitive conduct that substantially lessens competition in two or more MS.
- (iii) Regional rules and authorities are replacing functioning competition laws and authorities in MS before the RCA is fully operational; the preference of the current author and many other authors is that regional and MS laws and authorities should function in parallel in a complementary and coordinated manner.
- (iv) Industry, professional, occupational and other exemptions and exceptions from the region-wide rules are granted too often and too easily; competition law practitioners contend that such exemptions and exceptions should be limited to the greatest degree possible, and should be difficult to acquire by vested interests and relatively easy to remove when warranted.

Previous RTA experience also indicates that regional case selection, investigation, decision making and other processes should be designed to minimise the risk that regional competition activities and decisions systematically favour the interests of the larger and more highly developed MS at the expense of the smaller economies and their firms, industries and consumers. Distributions of benefits and costs that are perceived as unfair will discourage smaller, less advanced, and other members from participating in and contributing to the regional regime – even when they are receiving some benefits.

Other insights and possible lessons of a more general nature from studies of existing RTAs include the following:

- Regional and MS regimes and authorities that cover the anticompetitive conduct of both private and public undertakings are likely to be more effective and receive greater stakeholder support.
- The regional entity responsible for the RTA's competition obligations should be appropriately resourced and structured; and should be placed in a location that is accessible to other MS and will attract and retain high quality personnel.
- Binding and non-binding commitments under the RTA should minimise the risk that competition obligations impose information collection, analytical, investigation and related standards that are overly complex and burdensome and difficult to achieve by inexperienced and under-resourced national authorities.
- Overlapping membership whereby countries are members of more than one RTA has to date been mainly a theoretical concern, but could become more problematic as regional markets become more integrated, regional commissions are more active, and MS more often use regional enforcement cooperation platforms to address cross-border matters<sup>1</sup>.
- To be effective and sustainable over the longer term, the regional regime requires understanding, support and commitment from all MS governments and their business communities and other stakeholders.

One final lesson from these assessments is that the expectations of MS, their governments and business communities, and other interested parties and stakeholders should be appropriately managed from the outset; and false expectations and promises that all MS and stakeholder groups will benefit from all regional competition decisions should be avoided. Regional decisions will benefit some MS more than others, and some MS may experience or perceive they experience detriment – especially when the MS and its companies are the source and major beneficiary of ‘beggart-hy-neighbour’ anti-competitive conduct within the region. The MS losers can theoretically receive financial and other compensation from the “winners”, but this rarely occurs in practice.

## Key Lessons and Questions When Selecting the Regional Competition Rules Model

### Lessons Learned

These more positive insights from the RTA competition literature indicate that “the art of the possible” and incremental step-by-step approaches, which build success and minimize the risk of early failure, are important to designing and applying regional competition rules and obligations. Under a step-by-step approach, RTAs could first adopt a more informal regime to build the foundation for a more formal model in the future. This is the recommended approach of some assessments of the current SADC system, and has been proposed as the next step for ASEAN.

However, such an approach could have its own downside risks. The time, energy, attention span, and scarce cognitive resources and political support needed for members to design and reach consensus on more formal regional rules, mandates, scope and functions, may be better allocated to building competition law experience, credibility and legitimacy through better enforcement of existing national laws and developing and establishing effective enforcement cooperation platforms between member states.

When considering a more comprehensive and formal “hard law” model, regional authorities, proponents, and external advisors should recognize that MS and their CAs, business communities and other stakeholders have made major investments of time, energy and money in the current regime and can be quite satisfied with its performance – even though a “superior” option is now on offer.

Attention should also be given to possible trade-offs between different forms of convergence whereby, near perfect convergence in the objectives, provisions, and language of MS competition laws, can lead often unintentionally to divergences in enforcement practices, analytical methods, compliance and performance because of the ‘poor fit’ for some MS. One model out of the various regional competition options that are now available should not be seen as superior in all contexts, and as the inevitable final stage in the evolution of the RTA competition rules process.

On the one hand, the more formal EU model can potentially enhance regional competition law efficiency and effectiveness through:

- pooling resources and removing duplication, overlap and inconsistencies between MS;

- economies of scale and scope in enforcement, compliance promotion, education, and advocacy, and related positive externalities;
- extending the regional and global reach, visibility and credibility of national and regional competition rules;
- providing more consistent and effective remedies;
- reducing the transactions, regulatory and other costs and burdens of government, private, and other stakeholders; and,
- reducing political pressures from national interest groups.

On the other hand, achieving these potential benefits and advantages has been challenging for some RTAs; and “imposing” the EU model on reluctant MS may threaten existing domestic and RTA regimes that are now generating reasonably satisfactory compliance, enforcement, advocacy, and other outcomes through:

1. national competition regimes that have some “common ground” but are tailored to the socioeconomic and institutional conditions and stage of development of each member;
2. bilateral and multilateral enforcement cooperation between MS on an as needed basis to address cross-border matters;
3. and shared interests, information, learning, experience, mental models, trust, and reciprocity of trust involving MSCAs, the RCA, and other stakeholders.

The “imposition” of region-wide rules and authorities could also be used as an excuse by member governments and MSCAs to reduce their resources and enforcement efforts, and for MS without national competition laws and authorities to further delay.

Finally, the co-existence of different and competing regional competition systems operating in parallel and involving some of the same MS provides opportunities for experimentation, innovation, comparative systems analysis and shared learning for RTAs, developing economies and their external advisors. Competition, innovation and diversity are desirable in most contexts – including between regional competition regimes.

### **Ten Key Questions**

Prior to when a new RTA is established and before an existing RTA and its MS decide to move “up-scale” and adopt a more formal model,

the following ten questions should be addressed and answered to the extent possible:

1. How many MS have functioning competition laws and authorities and practical experience with case selection, investigation, analysis, and sanctioning anti-competitive business arrangements and practices?
2. Are the larger MS with significant competition law experience fully supportive of the regional competition rules and authority – and therefore prepared to accept the perceived and actual loss of national sovereignty, independence and control over key markets and sectors?
3. How similar and different are the MS competition objectives, policies, laws, standards, functions and enforcement practices; and how much convergence would be needed to reduce these differences and make regional rules and authorities functional and effective in achieving national and regional competition, consumer welfare, market integration, and other objectives?
4. Can this degree of alignment and convergence be achieved in the short to medium term to allow the regional rules and authority to be established and appropriately tested, evaluated, and modified where required, and placed on a positive trajectory?
5. Is there sufficient market integration and cross-border trade within the region to generate the number and quality of cross-border and regional enforcement cases and related matters, which would be needed for the RCA to develop experience, expertise, visibility, credibility and legitimacy among MS governments, CAs, businesses, and other stakeholders within the region, as well as governments, CAs, corporations and other stakeholders outside the region?
6. Is there reasonably strong empirical evidence that existing more informal bilateral and multilateral instruments between members have failed to deter, remedy and prevent some cross-border cartels, anticompetitive mergers, dominant positions, and other anticompetitive conduct?
7. Has consensus developed on easy to understand and apply guidelines on the scope of regional versus national rules; and the allocation of cartel, merger and other enforcement and related matters between

national and regional levels – in order to minimize conflicts between jurisdictions and promote transparency, certainty, compliance and enforcement across the region?

8. Is the consensus on these guidelines and related issues on jurisdiction, enforcement practices and competencies, and extraterritorial application likely to be stable and sustained across MS, regional entities and other stakeholders?
9. Are the regional competition rules and functions on offer expected to support and help to achieve the broader economic, social and institutional goals of the regional community and its members on:
  - inclusive growth and development and greater equality of opportunities, incomes, wealth and consumer and producer welfare;
  - sustainable development goals and other broader socioeconomic goals and objectives;
  - fair and efficient markets, fair competition and trading practices, legal and regulatory processes that are fair, transparent, open to all, and consistent with due process, and reduced rent seeking and corruption;
  - poverty alleviation, and the establishment and growth of micro-enterprises and other smaller enterprises within member states and the total region;
  - innovation, technological change, and institutional change; and,
  - a level playing field between private and state-owned enterprises?
10. Are the human resource and leadership skills, and MS financial, political and other commitments, needed to sustain a regional regime, available now and in the future?<sup>2</sup>

Many of these questions recognise that establishing, operating and sustaining a regional competition regime – which encompasses many MS at different stages of development — requires much stronger technical, management, negotiation, political, and leadership skills and savvy than establishing domestic regimes. Regional regimes need to accommodate: (i) mixed and conflicting influences, incentives, signals, and pressures from various government, business, civil society, and other groups; and (ii) distinctive national characteristics, values, philosophies, experiences and interests that are embedded within and ‘absorbed’ into MS competition

policies and laws and the enforcement, compliance promotion, advocacy, education and other practices and priorities of MSCAs.

Negative responses to and/or limited evidence on the majority of these questions may suggest that the potential net benefits from establishing a new regional competition regime or moving “up-scale” based on the modified EU model might be less than expected and required. Transplanting any regional competition rules model to a developing economy RTA requires considerable care and attention to the unique characteristics of the regional economy and its various member states; and to the mixed history and at times negative outcomes associated with transplanting advanced economy laws, regulations, and institutions with little modification from the developed to the developing worlds. While transplanting laws, regulations, rules and models is relatively easy, making them function effectively in developing economy environments can be more challenging.

Finally, advanced economy CAs, international organizations, and the academic community are often better positioned to provide advice and technical assistance to MSCAs than to RCAs – the consequence of the limited empirical evidence, comparative systems research, and shared learning on regional competition regime functions, limitations, and outcomes.

## **Concluding Comments and Proposals for Future Research**

Competition rules, obligations and objectives within developing economy RTAs have at times fallen short of expectations and predictions when compared with the EU and other developed economy RTAs. However, the “glass-is-half-full” approach adopted by this and other authors indicates many reasons for optimism in the future – especially if RTAs and their MS and external advisors take account of the full range of competition rules models that are available and select the model that best meets the current needs and stage of development of the regions and its member states.

The modified EU model has many attractive features; but the more informal and non-binding models can also generate net benefits for RTAs and their member states, particularly in regions where members display considerable socioeconomic and institutional diversity, and only some members have functioning competition laws and authorities. The ability of less formal arrangements to generate net benefits, and contribute to



competition and broader RTA objectives in a cost-effective manner, should be given appropriate weight by RTAs, their member states and external advisors when they are considering options for regional competition rules.

The Appendix provides an overview of currently available RTA information. This overview and other sources indicate that there are now close to 130 countries and jurisdictions in the global economy with competition laws and authorities, compared with about 30 mainly OECD economies only 25 years ago. These nearly 130 countries encompass the 34 current OECD members, and therefore the remaining more than 90 competition regimes are situated in countries that are typically categorised as developing, emerging market and/or middle income economies.

The Appendix identifies more than 80 countries that have functioning competition laws and authorities and are also members or associates of RTAs. The implication is that close to 50 of these MS are not OECD economies and therefore can be characterized as developing, emerging market and/or middle income countries. Therefore, the majority of the 90 plus developing and emerging market economies with functioning competition laws and authorities are either members of or are associated with one or more RTAs – while some others have bilateral trade and other agreements that may include competition obligations such as under Conton and other partnership agreements with the EU.

Anecdotal evidence, limited data, and the impressions of this and other RTA authors suggest that developing and emerging market CAs in countries that are members of one or more RTAs appear on average to be better resourced and funded and more effective than developing economy and emerging market CAs in non-RTA countries. However, this “impression” should be subjected to much greater ex-ante and especially ex-post research to confirm the benefits of RTA membership for MS and regional economies and their competition authorities and regimes; and to better determine the existing RTA competition rules models that best meet the needs of members and regions at different stages of economic and institutional development.

Additional ex-post RTA evaluations and related research are especially needed to identify and assess:

1. Specific enforcement cases and other competition matters where RTA information sharing and enforcement cooperation platforms resulted in higher quality decisions and outcomes for MSCAs and their economies.
2. Specific cross-border and other merger, cartel, AOD etc. enforcement cases that could not have been investigated and remedied without an

RCA with formal enforcement powers and capabilities under the modified EU model – because of e.g. the complexity or political sensitivity of the enforcement case for the member states and their competition authorities.

(i) Performance indicators for and empirical evidence on RTA competition regime progress, outcomes and successes that go beyond the number of enforcement cases and other inputs and activities to encompass progress, improvements and successes in such areas as:

- Business rivalry, competitive intensity, corporate culture, compliance promotion, and alternative case resolution through e.g. successful implementation of voluntary compliance action plans by regulated entities.
- Competition policy and law education and advocacy efforts within MS, at the regional scale, and at multilateral fora – including on the interactions between competition, trade, consumer policy, intellectual property, innovation, sectoral regulation and related matters.
- MS cooperation and information exchange – including the extent to which RTA platforms and RCA enforcement capabilities reduce the number, cost and complexity of regional and national enforcement cases.
- Promoting fair, efficient and more open economies within and across member states, including competition policy and law and related regulatory and procurement processes that are deemed to be fair, efficient, transparent, and consistent with due process.

Leading perhaps over time to more inclusive growth, greater equality in incomes, wealth and opportunities, and substantial reductions in corruption, rent-seeking and other harmful opportunistic conduct and perverse ‘social norms’ within MS and the total region.

- And key empirical evidence, findings and lessons from ex-post research on specific RTAs that can be extended to other regional trade agreements and can also be used to strengthen arguments for and help to determine the appropriate competition rules and obligations for multilateral competition rules under the WTO architecture.

3. The potential for RTA competition regimes to better identify and exploit the linkages between competition policy, law and consumer protection policy, law and advocacy.

Through e.g. the regional authority identifying enforcement matters and investigating cases where the alleged perpetrators are employing various forms of deception and misrepresentation to mislead consumers, business customers, competitors, and competition authorities in order to exploit their market power and strengthen cartels, dominant positions and other anticompetitive arrangements.

4. Ex-post empirical evidence which recognises that the enforcement of regional competition rules and obligations can result in both national and corporate “winners and losers” at least for the short-term.

This research would be designed to identify situations where the efforts of member states to “protect and compensate” their national corporate ‘losers’ impeded national and regional competition, trade, economic efficiency, competitiveness and innovation over the longer term.

As well the alternative situations where the member state ‘losers’ agreed with or at least did not attempt to impede and offset the effects of the regional competition decision, and thereby benefited from a stronger and more competitive national and regional economy over the longer term.

This resulted in substantial increases in both consumer and producer surplus at the national and regional levels and important contributions to broader national and regional development objectives (that are listed earlier).

5. The potential for innovative and effective ‘mid-way points’ between the more formal and informal RTA models described in this Paper – for example through providing an existing regional legal institution with the mandate to investigate and adjudicate especially important, complex, large and politically sensitive cross-border enforcement cases and other matters that cannot be successfully addressed by member state competition authorities (MSCAs).
6. Benefits to regional trade and national and regional economies, competitiveness, productivity and innovation, through employing RTA competition obligations to replace anti-dumping laws with competition rules and to use competition rules to discipline state aids/subsidies, state-owned enterprises, government procurement practices, and other anticompetitive government administrative practices and interventions.

7. And the extent to which incorporating competition rules and obligations in RTAs help the member states and total region to better employ competition policy and law to achieve more inclusive growth, sustainable development goals and other broader socio-economic and public welfare goals and objectives of member states and the total region through for example:

- Enhancing the competition policy research and advocacy efforts of member state CAs and other ministries and departments, civil society groups, business community, and the academic community.
- Addressing cartel, collusion, bid-rigging, abuse of dominance and other enforcement matters involving anticompetitive conduct that especially harms more vulnerable and disadvantaged economic actors: final consumers, small farmers, small and micro-enterprises, governments and their taxpayers in smaller member states etc.
- Applying a more holistic value and supply chain approach which identifies and remedies potentially anti-competitive conduct and arrangements at different stages of value chains – regardless of the member state where the anticompetitive conduct and impediments to enhanced consumer and producer welfare is taking place.
- And better demonstrating and providing strong empirical evidence on the positive and negative interactions between trade and competition policies and why trade liberalization requires competition policy and law reforms at the member state and regional levels.

Perhaps most importantly, ex-post research of existing RTAs with competition rules and obligations and *ex-ante* research of proposed RTAs should be conducted on the potentially positive dynamic, interactive, feedback, and path dependent effects between, on the one hand, the benefits that RTAs and their national and regional economies receive from their regional and national competition rules and obligations; and on the other hand the benefits that national competition regimes and authorities receive from incorporating competition rules and obligations within regional trade agreements.

This research should include the learning, network and path dependent effects and benefits and related positive network externalities that result from the interactions between the different RTA competition law ‘platforms and networks’ (which in some cases have overlapping membership); and between the RTA platforms and networks and the other competition policy and law networks and forums that are now fully

operational or are emerging – including the very unique, expanding and influential CUTS network of competition, consumer, and regulatory policy and reform experts and advocates from government agencies and ministries, international organisations, the academic community, civil society and other groups in both the developed and developing worlds.

## Appendix A:

### Overview of Competition Policy and Law Obligations and Progress in Selected Regional Trade Agreements (RTAs)

Regional Trade Agreement (RTA)	Member States (MS)	Formal and Informal Obligations of Member States (MS) under the RTA and Progress in Achieving Obligations and Objectives <sup>3</sup>
European Union (EU)	<p>28 member states, as well as five candidate countries and two potential candidate countries.</p> <p>Current members are: Austria, Belgium, Bulgaria, Croatia, Republic of Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden and the United Kingdom</p>	<p>EU wide competition rules and enforcement have been in place since the Treaty of Rome of 1957, and are administered and enforced by the Competition Commission in Brussels. EU competition rules include anti-competitive agreements and forms of abuse of dominance by private undertakings in Articles 101 and 102 of the Treaty on the Functioning of the European Union (TFEU) of 2007, the EU Merger Regulation, and competition policy rules on the behaviour of public undertakings and state aids (subsidies).</p> <p>There are as well formal obligations for current and new member states and for prospective members to develop and enforce competition laws that are similar to EU wide rules, and to cooperate with each other and with Brussels when enforcing their national competition laws. All current EU members have established competition policies, laws and authorities and are meeting their EU competition law obligations.</p> <p>In addition, under the European Economic Area (EEA) negotiated with the European Free Trade Association (EFTA), EFTA members are expected to adopt EU competition rules and standards, and similar competition obligations are contained in EU agreements with Eastern and Central European and Mediterranean countries that are not EU members.</p> <p>Finally, the Cotonou Agreement between the EU and the African, Caribbean and Pacific countries, which was signed on 23 June 2000 and entered into force on 1 April 2003, includes Article 45 on the introduction and implementation of effective and sound competition policies and rules by the parties to the Agreement. In sum, EU agreements with non-member partners include commitments to apply common standards and disciplines in such areas as antitrust/competition law, state aids and state monopolies (Hoekman 2002:6-10).</p> <p>The RTA competition policy and law literature indicates that the EU competition rules system has had greater enforcement success than any other regional competition policy and law system; and has been promoted widely and with considerable success to other RTAs — with the result that most but not all RTAs with regional competition rules and obligations have adopted some form of the EU model (see e.g. Botta 2011 and Marquis 2015).</p>
North American Free Trade Agreement (NAFTA)	Three members: United States, Canada, and Mexico	There are formal obligations in the NAFTA Treaty for all three parties to develop and enforce competition laws and to cooperate with each other when enforcing their national laws. There are no formal obligations to develop regional competition rules and/or ensure similarity, convergence and harmonization of competition laws, rules, standards and enforcement practices.

Regional Trade Agreement (RTA)	Member States (MS)	Formal and Informal Obligations of Member States (MS) under the RTA and Progress in Achieving Obligations and Objectives <sup>3</sup>
		<p>However, the NAFTA literature and developments over the past two plus decades indicate that informal processes of ‘soft’ convergence and alignment of objectives, enforcement practices and analytical methods are taking place through frequent bilateral contacts and other contacts and cooperation at multilateral forums: OECD, ICN etc. – including what is called “pick-up-the-phone” personal relationships. All three members are complying with their treaty obligations and contributing to informal processes and platforms of information sharing, enforcement cooperation, positive comity, and soft convergence in competition policy, law, and enforcement practices (see e.g. Hoekman 2002, footnote on page 13, Crawford 1997, and Aydin 2015).</p> <p>Mexico’s competition authority, the Federal Competition Commission, generally receives high marks from the OECD and other groups for the quality of and recent improvements to its enforcement, competition advocacy and education, and related functions – in particular for its recent enforcement and other efforts to reduce anticompetitive practices in value chains that supply essential food and other products to lower income and other consumers and households (OECD 2012:31-36 and Aydin 2015).</p>
Closer Economic Relations Agreement (ANZCERTA or CER)	Australia and New Zealand	<p>Signed in 1983, ANZCERTA required the two countries to examine the scope for taking action to harmonize the CER requirements that relate to restrictive trade practices. This started a process of convergence largely through changes in New Zealand’s competition law in order to facilitate the elimination of antidumping on the two countries’ bilateral trade flows, which occurred in 1990.</p> <p>At the same time, controls on subsidies that distort trade and competition within the free trade area were established; and soon after domestic competition law prohibitions on the misuse of market power were extended to trans-Tasman markets. Moreover, measures to coordinate the enforcement of competition law are now in place between the two countries.</p> <p>As summarised by Hoekman (2002:10): “in the ANZCERTA context full trade liberalization was judged necessary but not sufficient to eliminate the need for antidumping. Such elimination required active enforcement of <i>similar</i> competition laws and agreement that the jurisdiction of competition agencies extend to matters affecting trade between New Zealand and Australia.</p> <p>In this connection it was agreed that nationals of one state could be made the subject of an enquiry by the competition authorities of the other state and be required to respond to requests for information. Australian (New Zealand) antitrust legislation was amended to extend its scope to the behavior Australian and/or New Zealand firms with market power on either one of the national markets or the combined Australia/New Zealand market; Courts were empowered to sit in the other country; orders may be served in the other country; and judgements of Courts or authorities of one country are enforceable in the other country. In 1994 the competition authorities of the two countries concluded a bilateral Cooperation and Coordination Agreement to reduce the possibility for inconsistencies in the application of legislation in instances where this is not required by statutory provisions ...”</p>

Regional Trade Agreement (RTA)	Member States (MS)	Formal and Informal Obligations of Member States (MS) under the RTA and Progress in Achieving Obligations and Objectives <sup>3</sup>
		<p>Accordingly, the two countries still have their own competition laws and authorities, but have developed the cooperative and coordinated approaches and platforms needed for a single economic market, mainly through active and proactive bilateral informal, as needed, and ad hoc cooperation based on legislation, agreements, arrangements and ongoing informal links. The success of this approach has been recognized by the OECD as a best-practice international model. The consensus is that, except for the European Union, the CER has made the greatest progress with using competition policy and law and related regulatory reform, alignment and cooperation measures in order to promote a single market within the CER RTA and region – while employing a more informal model.</p> <p>What is interesting and provocative is that the CER made this substantial progress through an interesting mix of binding and non-binding commitments and without fully adopting the EU model of regional competition rules, a regional commission, and regional supremacy over national rules and authorities.</p> <p>Whether this alternative model involving two advanced OECD economies at broadly similar stages of development and close political and economic relations could be extended to RTAs – which encompass many developing economy member states at very different stages of economic, social and institutional development and with different competition and other economic objectives and priorities – is an unanswered question that requires more theoretical and empirical ex-ante and especially ex-post research and policy analysis.</p>
Mercosur (the Southern Common Market)	<p>Argentina, Brazil, Paraguay, Uruguay and Venezuela are full members.</p> <p>Chile, Bolivia, Colombia, Ecuador and Peru are associate members, and New Zealand and Mexico are observers</p>	<p>There was no competition chapter in the Mercosur Treaty of 1997, but the Fortaleza Protocol of 1997 established a regional competition policy to be applied to anticompetitive behaviour that has an impact on intra-block trade. All Mercosur members and associates now have competition laws and authorities — with the exception of Bolivia, which however has some provisions on competition and unfair trading practices in its constitution and in other statutes. Paraguay was the most recent member state to enact a competition law in 2014.</p> <p>The Mercosur regime was originally based on a modified EU model, but with no merger control, no control of state aids, and no elimination of intra-block anti-dumping duties. In addition, Mercosur has an inter-governmental framework of enforcement, which led to questions regarding the supremacy of the region-wide rules and CA.</p> <p>The agreement based on the EU model was ratified by only two MS, Brazil and Paraguay, even though Paraguay had no competition law and authority at that time, and ratification by the other MS was highly doubtful. Therefore, the EU model has been replaced by more modest information sharing and enforcement cooperation agreements first between Argentina and Brazil in 2003, which was then extended to all MS. It is reported that the revision process was fully completed in 2010 (Araujo 2001, Cotta 2011:8-17 and OECD 2012 on Brazil, Argentina and Chile).</p> <p>Limited progress with Mercosur competition rules is reportedly the result of ideological differences and limited cooperation and trust between member states and their competition authorities, limited</p>



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		<p>competition law resources and experience of some MS authorities, and arguably the adoption at the outset of a Mercosur system that was too complex, ambitious and challenging — which was “doomed” to fail because of the above considerations and other conditions and constraints.</p> <p>In addition, the Mercosur experience suggests that starting with a very challenging and arguably too ambitious regional regime, which requires a high degree of competition law experience, commonality, cooperation and consensus across MS from the outset, may be problematic for some RTAs. A phased step-by-step approach that begins with a less ambitious regional competition model and system may be preferable.</p> <p>Among other considerations and risks, early failure with a more ambitious model may place RTA competition rules and authorities on a negative development path and trajectory that can hinder, complicate and even undermine the later adoption of a less challenging and more informal “best-efforts” or other RTA model. However, this presumption should be the subject of future ex-post research.</p>
Andean Community	<p>A trade bloc of four countries: Bolivia, Colombia, Ecuador and Peru.</p> <p>Chile, Argentina, Brazil, Paraguay and Uruguay are associate members and Panama, Mexico, and Spain are Observers.</p>	<p>Three of four full members have competition laws and authorities – as noted above, the exception is Bolivia. The Ecuador authority was established in 2012 and its competition law was enacted in 2013. The Community has received financial and technical assistance from the EU to establish its regional competition law framework, and reportedly has adopted the EU approach to Community wide competition rules (Marquis 2015:17). Under Articles 93 and 94 of the Cartagena Agreement, the Andean Community adopted Decision 285, which has the objective of preventing or correcting distortions in competition that are caused by restrictive anticompetitive practices and covers agreements, concerted practices or parallel actions among competitors, and the abuse of a dominant position (Ferreira 2005).</p> <p>Under the current regional system, the enforcement of the region-wide Community rules is limited to cases with an impact on intra-regional trade and therefore local anti-competitive practices are investigated and sanctioned under national competition laws. However, Bolivia (and Ecuador until 2013) can apply the Community rules domestically until national laws are in place. Botta (2011) concluded that the Andean Community has an effective regional competition policy in terms of both its substantive provisions and its enforcement system, which is considerably better than the regional competition policy and law regime in Mercosur.</p> <p>However, despite the improvements in the institutional framework, the extent of enforcement is reported to be disappointing – the consequence of: (i) the trade effects doctrine combined with the limited market integration and cross-border trade within the Community, (ii) the non-supportive political climate in some MS where e.g. some MS see competition law as an instrument to regulate and control prices rather than to promote the competitive process and fair and efficient markets, (iii) the long list of exceptions to the region-wide rules, and (iv) continuing questions regarding the supremacy of region-wide rules in the Community (Botta 2011:17-25; see as well OECD 2012 on Peru, Columbia and Chile and Beneke 2015).</p>

Regional Trade Agreement (RTA)	Member States (MS)	Formal and Informal Obligations of Member States (MS) under the RTA and Progress in Achieving Obligations and Objectives <sup>3</sup>
		<p>One issue for future research is that Chile, which is one of the more advanced economies in South America and has an experienced competition authority, is only an associate member of Mercosur and the Andean Community (see e.g. OECD 2012 and Roberts and Tapia 2013). At the same time, Chile has free trade agreements with a quite large number of developed and developing economies and jurisdictions, which often include competition provisions, is a member of APEC, and is one of twelve countries that is participating in the negotiations on the Trans-Pacific Partnership Free Trade Negotiations which are now very close to completion and MS approval (discussed below)<sup>4</sup>.</p> <p>Future research could address whether full participation by Chile in Mercosur and the Andean Community would have strengthened their national and regional competition policy and law initiatives – in light of the possibility that Chile could have played more of a leadership role similar to South Africa's contribution in SADC.</p>
Caribbean Community (CARICOM)	<p>15 full member states, 5 associates, and 8 observers. The 15 full members are: Antigua and Barbuda, Bahamas, Barbados, Belize, Dominica, Grenada, Guyana, Haiti, Jamaica, Montserrat, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Suriname, and Trinidad and Tobago.</p> <p>The OECS sub-region within CARICOM is comprised of (with populations in brackets for the latest year available): Antigua and Barbuda (89,138), Dominica (69,810),</p>	<p>With a relatively few important exceptions, CARICOM is largely comprised of small island nations which have less developed economies, and do not have the resources and administrative capacities to establish and administer their own competition rules and authorities (Stewart 2004 and Botta 2011). Therefore, the EU competition model and rules adopted by CARICOM focused on region-wide (supranational) rules and a regional competition authority, and prohibitions against anticompetitive practices and abuses of dominant position are being applied.</p> <p>However, regional competition law progress, enforcement, and positive outcomes have been limited by:</p> <ul style="list-style-type: none"> <li>(i) less than expected and desired economic integration and intra-CARICOM trade flows;</li> <li>(ii) major differences in economic and institutional development between CARICOM member states;</li> <li>(iii) continuing tensions between MS national sovereignty concerns and regional integration “aspirations”;</li> <li>(iv) a multi-level system of enforcement which requires consultation and cooperation between relevant MS and the CARICOM Competition Commission (CCC) before the CCC can impose a fine on a private undertaking;</li> <li>(v) the failure of many MS that may have the resources to establish their own national competition authorities;</li> <li>(vi) limiting the region-wide competition rules to anticompetitive conduct that affects intra-regional trade, which does not allow the regional authority to address potentially anti-competitive conduct and arrangements that could be harming competition, economic efficiency, consumers and other market participants in two or more MS; and,</li> <li>(vii) continuing questions on the scope and supremacy of region-wide competition rules.</li> </ul> <p>The available information indicates that only Jamaica and Barbados have complied with the CARICOM obligation and now have functioning competition laws and authorities.</p> <p>As well, the competition law of Trinidad and Tobago has been approved but has not been fully enacted; Suriname is consulting on a</p>

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	Grenada (110,821), Montserrat (4,681), Saint Kitts and Nevis (51,967), Saint Lucia (172,034), and Saint Vincent and the Grenadines (100,596).	<p>draft competition bill; the OECS sub-region has completed an agreement and draft competition bill; and Belize has prepared a strategy for competition policy and law implementation.</p> <p>As a result, as of 2011 or ten years after the Treaty to establish the CCC was signed, the Commission had no cases that resulted in the enforcement of the CARICOM competition rules (Botta 2011, Beckford 2009, Kaczorowska 2012, and CCC 2013).</p> <p>Despite these limitations, the decision of the smaller nation states in the OECS sub-region to work together and establish a sub-regional competition law and authority should be considered as a potential international “best practice” which should be followed closely in the future for application by other smaller states and “micro-states” in the global economy such as the smaller countries and micro-states in the South Pacific (see e.g. Reddy 2013 on the limited development to date of functioning competition laws and authorities in the Pacific Region).</p>
Common Market for Eastern and Southern Africa (COMESA)	19 member states: Burundi, Comoros, Democratic Republic of the Congo, Djibouti, Egypt, Eritrea, Ethiopia, Kenya, Libya, Madagascar, Malawi, Mauritius, Rwanda, Seychelles, Sudan, Swaziland, Uganda, Zambia and Zimbabwe	<p>This RTA has adopted the EU model with COMESA wide competition rules enforced by the COMESA Competition Commission (CCC) in Lilongwe Malawi. COMESA competition law and commission became fully operational in January 2013. The COMESA competition law includes provisions on restrictive business practices, prohibited practices, abuse of dominant position, merger control, and consumer protection – as well as authorizations whereby undertakings can apply to the CCC for authorization of potentially anticompetitive activities on the basis that the public benefits outweigh the anticompetitive detriment.</p> <p>There are as well formal obligations in the COMESA Treaty for each member state to have a modern competition policy and law that is similar to and aligned with COMESA wide rules. 14 of 19 COMESA members now have competition laws, the other five are now drafting their competition laws, and ten of nineteen MS now have functioning competition authorities including six which are also members of SADC (see below).</p> <p>Furthermore, Kenya, which has one of the more experienced competition authorities in COMESA and Africa, is also a member of the EAC (discussed below). Therefore, 7 of the 10 COMESA members that have functioning competition laws and authorities are also members of other RTAs<sup>5</sup>.</p> <p>COMESA likely has the most developed and well-articulated regional competition regime of any RTA in Africa and has one of the most highly developed among all of the developing economy RTAs in the global economy. Its Competition Commission is led by a well-known and highly experienced and influential Director and Chief Executive Officer, who previously was the agency head of the Zambian competition authority.</p> <p>As a consequence, the COMESA competition rules and authority has received a great deal of attention (both positive and negative) from the business, financial, and general media, international institutions, the legal community, and other sources (see e.g. Rudman and Wilson 2013, Coulson Harney and Slaughter and May 2013, and The Antitrust</p>

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		Source 2014). Its progress, successes, and alleged and actual “shortfalls” on merger review and other provisions will be closely monitored and reported on in the coming years; and as well will provide important ex-post evidence for future research on the strengths and weaknesses of different RTA competition regimes and models.
Southern Africa Development Community (SADC)	<p>15 member states: Angola, Botswana, Democratic Republic of Congo, Lesotho, Madagascar, Malawi, Mauritius, Mozambique, Namibia, Seychelles, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe.</p> <p>Note that eight SADC members are also in COMESA, and Tanzania is also in the EAC (below).</p>	<p>There are no formal competition obligations in the SADC Treaty, but MS have made best-efforts commitments to develop and enforce competition policies and laws and to cooperate when enforcing these laws. These commitments have been incorporated into many major legal and policy documents signed by SADC Heads of States and Governments including the Protocol on Trade in 2002, the Regional Indicative Strategic Development Plan of 2003, the Protocol on Finance and Investment in 2006, and the Declaration on Regional Cooperation in Competition and Consumer Policies of 2009.</p> <p>At the present time, 11 of 15 SADC member states have competition laws and fully operational competition authorities, Madagascar enacted a competition law in 2005 that is not yet in effect; Lesotho has prepared a draft competition law, and one of the purposes of the country’s Privatization Act is to promote competition and reduce monopolistic behaviour; and the two remaining member states, Angola and DR Congo, are reported to be at an early stage of competition law development.</p> <p>Therefore, the member states with functioning competition laws and authorities are South Africa, Zimbabwe, Zambia, Malawi, Tanzania, Namibia, Mauritius, Swaziland, Seychelles, Botswana in 2011, and most recently Mozambique in 2013, with a competition law that is inspired by the laws and rules in Brazil, Portugal, other European countries, and the European Union. The 11 SADC member states in 2015 represent major progress in a relatively short period of time since only three MS: South Africa, Zimbabwe and Zambia, had fully functioning competition laws and authorities in 2004.</p> <p>Six of the eight SADC members that are also members of COMESA have competition laws and authorities. Moreover, five SADC member states are also members of the Southern African Customs Union (SACU) which also has informal competition obligations. The five SACU member states are Botswana, Lesotho, Namibia, Swaziland and South Africa. Based on the available information, within SACU, only Lesotho does not currently have a functioning competition law and authority.</p> <p>Unlike COMESA, there is strong opposition, mainly from the non-COMESA member states in SADC, to establishing region-wide SADC competition rules and a regional commission. One important regional constraint is that only one SADC Secretariat officer has been designated to coordinate and manage regional competition issues across the 15 MS.</p> <p>Nonetheless, the regional competition entity with the support of the EU and other donors has provided advice, assistance and support to existing CAs and the establishment of new CAs in the areas of for example: (i) competition policy and law best practices, (ii) information sharing and enforcement cooperation platforms, (iii) specific</p>

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		enforcement cases with cross-border ramifications, (iv) assistance with international competition forums and networks, and (iv) the linkages between competition and consumer protection policies, laws and advocacy (Khandelwal 2004, Gal and Wassmer 2012, Senona et al 2013 and Ireland 2012).
East African Community (EAC)	Five member states in the African Great Lakes Region of eastern Africa: Burundi, Kenya, Rwanda, Tanzania, and Uganda	<p>The East African Community Competition Act was developed and approved in 2006 and contains sections on restraints by enterprises, abuse of market dominance, mergers and acquisitions, state subsidies, public procurement, enforcement procedures, consumer welfare and protection, and establishment of the East African Competition Authority.</p> <p>The regulations to administer and enforce the Act were developed and approved in 2010, but progress with implementing the law and regulations has been slow — reportedly because of limited awareness of the importance of competition policy and law within the EAC region, and because for a long time one of the five member states, Uganda, had not adopted the EAC law. However, the EAC Council of Ministers decided that the law should become operational by December 2014 bringing to an end an eight-year delay; and other media reports indicate that the EAC competition authority would become operational by mid-year 2015. However, more recent reports suggest that the establishment of the EACCA may occur later in 2015 or early in 2016; and that as of December 2015 the EAC competition authority was still not fully functional<sup>6</sup>.</p> <p>The RTA literature and media reports indicate that among the five member states, Kenya and Tanzania have the most competition law experience. Burundi's competition law and authority were established in 2010 but were not fully operational as of 2014. Rwanda has competition rules in various statutes, including the Competition and Consumer Protection Law; and the authority to administer enforce that law will reportedly become operational sometime in 2015.</p> <p>Uganda drafted a competition law in 2004, which was then revised in 2007, but as of 2014 the proposed law had not yet been approved by the Uganda Parliament and then enacted and enforced; however media reports in 2014 indicate that the Uganda Cabinet would soon approve the competition bill, and pass on the bill for debate and approval in Parliament; the bill would create an independent body called the Uganda Competition Commission.</p> <p>As noted above, Kenya, Uganda, Burundi and Rwanda are also members of COMESA, and Tanzania is a member of SADC and was previously a member of COMESA (see e.g. Angwenyi 2013 regarding the challenges of multiple RTA memberships with overlapping competition law jurisdictions, and the Tripartite MOU between COMESA, EAC and SADC signed in 2011)<sup>7</sup>.</p>
Economic Community of West African States (ECOWAS)	15 members: Benin, Burkina Faso, Cabo Verde, Côte D'Ivoire, The	ECOWAS was established in 1975. Articles 50 and 60 of the ECOWAS Treaty provide the legal basis and justification for a competition policy for ECOWAS; and the formal and informal competition policy obligations and requirements of ECOWAS member states are described in its "Regional Competition Policy Framework" document which was completed in 2007.

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	Gambia, Ghana, Guinea, Guinea Bissau, Liberia, Mali, Niger, Nigeria, Senegal, Sierra Leone, and Togo	<p>This framework has six segments on: (i) the objective and basic principles of a competition policy; (ii) justification of a regional competition policy for ECOWAS; (iii) current status of competition laws within ECOWAS; (iv) the main outlines of Community rules on competition within ECOWAS; (v) implementation conditions including preconditions for effective application of regional rules on competition; and, (vi) capacity building.</p> <p>The limited literature on ECOWAS competition policy and law indicates that meeting these obligations and requirements continues to be a “work in progress” (see e.g. Mathis and Dawar 2008; and Drexel et al 2012). For example, as of 2007, except for the WAEMU members noted below, the non WAEMU members did not have fully functioning competition laws and authorities at that time. The available information suggests that since then Gambia now has a competition law and commission and is making progress on the enforcement of its law; and Ghana, Nigeria, and Guinea have continued to work on draft competition policies and laws – with some evidence that through the work of CUTS and others some progress is being made in Ghana and Nigeria.</p> <p>The case of Nigeria, one of the largest and most important countries and economies in Africa, may be important in this regard. Nigeria has been drafting, debating, consulting on, and receiving outside technical assistance on a new competition law for a number of years and a new Federal Competition Bill was drafted a few years ago. However, more recent media reports indicate that, while Nigeria has competition provisions in some other laws especially in the Communications Act, the country still does not have a fully functioning competition law and authority (see e.g. Odion 2015)<sup>8</sup>.</p> <p>When one of the major economic leaders of an RTA is a competition law “laggard”, smaller and less advanced countries may have a good excuse for not developing and implementing their own competition laws and authorities. The Nigeria and ECOWAS situation can be compared with the leadership roles played by for example South Africa and Brazil in their respective RTAs and regional competition law communities. This situation is consistent with the insights from behavioral economics which illustrate how and why individuals, companies, other organizations and even countries tend to follow, imitate and learn from national and regional leaders.</p>
West African Economic and Monetary Union (WAEMU – also known as UEMOA)	8 member states: Benin, Burkina Faso, Cote d'Ivoire, Guinea-Bissau, Mali, Niger, Senegal, and Togo – all eight are also members of ECOWAS	<p>As of 2014, none of the WAEMU member states had implemented a national competition regime (see ECOWAS discussion above). The ECOWAS framework document of 2007 indicates that the WAEMU members of ECOWAS are covered by the WAEMU/UEMOA competition law obligations as set out in WAEMU's three regulations and two directives that were introduced in 2002 and came into effect in 2003.</p> <p>The three Regulations cover concerted anti-competitive practices, abuse of a dominant market position, and state aid, while the two Directives apply to (1) transparency in financial relations between Member States and public enterprises, and between Member States and foreign or international organisations; and (2) cooperation between the WAEMU Commission and national competition authorities. However, other</p>

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		<p>more recent sources suggest that these regulations and directives are not yet being effectively enforced (see e.g. Bakhoun and Molestina 2012 and Staples 2012).</p> <p>Some studies have indicated that one of the major lessons from the WAEMU competition policy and law experience is as follows: “The distribution of competences between the WAEMU Commission and the national competition authorities is the most contentious issue in the WAEMU enforcement approach. The centralization of the decision-making power has evidenced its limits. National competition authorities should enjoy the freedom to protect national markets by directly addressing national restrictions of competition” (Bakhoun and Molestina 2012:24; see as well Gal and Wassmer 2012:6 and Wieck 2010).</p> <p>This paper and appendix has noted some “best practices” for RTA competition regimes. Transferring competition rules enforcement from functioning national competition authorities to a regional authority that is not yet functioning and has limited resources should be considered as a lesson and “worst practice” to be avoided by RTAs in the future.</p>
Central African Common Market (CEMAC)	6 member states: Cameroon, Central African Republic, Chad, Republic of the Congo, Equatorial Guinea and Gabon	<p>As of 2014, CEMAC had not yet implemented a regional competition policy, and only Cameroon and Gabon had functioning competition laws, authorities and regimes. However, it is reported that expanding trade and economic activity in the CEMAC region may lead to greater interest in competition legislation and a regional competition policy among member states and stakeholders in the coming years.</p> <p>Limited progress appears related in part to limited resources and commitment at the regional level, where only two officials have the responsibility to deal with competition issues; and the CEMAC Competition Council is a temporary not a permanent body (see e.g. Gal and Wassmer 2012 and Staples 2012).</p>
Association of South East Asian Nations (ASEAN)	10 member states: Indonesia, Malaysia, Philippines, Singapore, Thailand, Brunei, Viet Nam, Laos, Myanmar and Cambodia	<p>The ASEAN Experts group on Competition was established in 2007; and a major commitment in the ASEAN Economic Community (AEC) Blueprint of the same year is that all ten member states need to introduce national competition policies and laws by 2015.</p> <p>Indonesia, Singapore, Thailand, Vietnam and Malaysia now have functioning competition laws and authorities; the Philippines Congress approved its Competition Act in June 2015; the Myanmar competition bill was approved and signed into law by the President in February 2015; and media reports and ASEAN documents indicate that Brunei Darussalam, Cambodia, and Lao PDR are currently drafting competition laws. In addition, a coordination mechanism for competition law enforcement across the ASEAN region is planned for development by the end of 2015 (Marquis 2015:17).</p> <p>The ASEAN Regional Guidelines on Competition Policy of 2010 are designed to provide guidance to ASEAN MS that have not yet developed competition laws and authorities, and to other MS that may be planning to improve their competition policy and law regime in the future. These guidelines and other regional measures are consistent</p>

Regional Trade Agreement (RTA)	Member States (MS)	Formal and Informal Obligations of Member States (MS) under the RTA and Progress in Achieving Obligations and Objectives <sup>3</sup>
		<p>with informal, soft law, organic convergence processes involving shared information, learning and mental models and imitation; and non-binding “MS best efforts” initiatives towards greater alignment and convergence of competition laws, rules and functions across ASEAN MS.</p> <p>ASEAN therefore has reportedly not adopted a modified EU model, and apparently is moving towards a regional competition model that is closer to the NAFTA and SADC models — based on: (i) competition laws in all MS, (ii) guidelines, education, and capacity building, (iii) intra-regional and extra-regional networking initiatives at the ASEAN regional level, and (iv) encouragement of information sharing, enforcement cooperation, and competition policy and law education and advocacy instruments and platforms between MS (see e.g. Wisuttisak and Binh 2012, Rodyk 2012, Lee and Fukunaga 2013, and the ASEAN 2013 Handbook on Competition Policy and Law for Business).</p>
Trans-Pacific Partnership (TPP) Free Trade Negotiations and Agreement	12 Countries: United States, Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, and Vietnam	<p>American documents indicate that the United States and some other countries have placed significant emphasis on stronger rules for competition and many other laws and regulations – including attention to the implications for: (i) regulatory coherence, (ii) supply chain competitiveness, (iii) “competitive neutrality” between state-owned and privately-owned enterprises to ensure that SOEs are not provided a competitive advantage by their governments compared with private enterprises; (iv) minimisation of regulatory and other non-tariff barriers to foreign markets; (v) minimization of regulatory and other non-tariff foreign barriers to market access and competition; and, (vi) increased participation of small and medium-sized enterprises in regional trade.</p> <p>“The November 2011 framework indicates that the TPP partners are discussing language for a chapter on competition policy to ‘promote a competitive business environment, protect consumers and ensure a level playing field for TPP companies.’ The text will include language ‘on the establishment and maintenance of competition laws and authorities, procedural fairness in competition law enforcement, transparency, consumer protection, private rights of action, and technical cooperation.’ The U.S. business community has indicated that the provisions on competition policy will be critical in dealing with state-owned enterprises (SOEs), particularly in addressing issues concerning their financing, regulation, and transparency, to ensure that they are not provided an unfair competitive advantage” (Fergusson et al 2015).</p> <p>Overview reports on the TPP Agreement indicate a separate chapter on competition policy and law provisions and references to competition in some other chapters in the agreement. The major features of the competition policy chapter are as follows.</p> <p>“TPP Parties share an interest in ensuring a framework of fair competition in the region through rules that require TPP Parties to maintain legal regimes that prohibit anticompetitive business conduct, as well as fraudulent and deceptive commercial activities that harm consumers.</p>



Regional Trade Agreement (RTA)	Member States (MS)	Formal and Informal Obligations of Member States (MS) under the RTA and Progress in Achieving Obligations and Objectives <sup>3</sup>
		<p>TPP Parties agree to adopt or maintain national competition laws that proscribe anticompetitive business conduct and work to apply these laws to all commercial activities in their territories. To ensure that such laws are effectively implemented, TPP Parties agree to establish or maintain authorities responsible for the enforcement of national competition laws, and adopt or maintain laws or regulations that proscribe fraudulent and deceptive commercial activities that cause harm or potential harm to consumers. Parties also agree to cooperate, as appropriate, on matters of mutual interest related to competition activities.</p> <p>The 12 Parties agree to obligations on due process and procedural fairness, as well as private rights of action for injury caused by a violation of a Party's national competition law. In addition, TPP Parties agree to cooperate in the area of competition policy and competition law enforcement, including through notification, consultation and exchange of information. The chapter is not subject to the dispute settlement provisions of the TPP, but TPP Parties may consult on concerns related to the chapter<sup>10</sup>.</p> <p>It appears therefore that the competition obligations do not adopt the more formal EU regional rules and enforcement; but go beyond the relatively simple NAFTA model through the direct references to consumer protection, economy-wide coverage which would address the commercial activities of state-owned enterprises and designated monopolies (addressed in a separate chapter), private rights of action, procedural fairness in competition law enforcement, transparency, and technical cooperation. Other chapters include references to steps to promote competition in international mobile roaming services. These competition policy and related provisions on competition could be just as important and consequential for competition in the TPP member states as the competition law chapter described earlier.</p> <p>One future development that could be a "game changer" for the TPP and for competition rules within RTAs is the possibility that the People's Republic of China could join the TPP in the not-too-distant future. Media and academic reports indicate that China continues to be an active and at times controversial enforcer of its relatively new Anti-Monopoly Law (AML) which started to be enforced in August 2008 (see e.g. Ng 2015).</p>
Asia Pacific Economic Cooperation (APEC)	21 members: Australia, Brunei Darussalam, Canada, Chile, People's Republic of China (PRC), Hong Kong China, Indonesia, Japan, Republic of Korea, Malaysia, Mexico, New Zealand, Papua	<p>There are no formal competition law obligations but APEC has given important attention to competition policy and law almost from the beginning in 1989. Established in 1996, APEC's Competition Policy and Law Group (CPLG):</p> <ul style="list-style-type: none"> <li>(i) promotes an understanding of regional competition laws and policies,</li> <li>(ii) examines the impact of competition policy and law on trade and investment flows,</li> <li>(iii) identifies areas for technical cooperation and capacity building among member economies,</li> <li>(iv) and maintains a Competition Policy and Law Database, which provides access to the various competition policies and laws that are in force within the 21 APEC member economies.</li> </ul>

Regional Trade Agreement (RTA)	Member States (MS)	Formal and Informal Obligations of Member States (MS) under the RTA and Progress in Achieving Obligations and Objectives <sup>3</sup>
	New Guinea, Peru, The Philippines, Russia, Singapore, Chinese Taipei, Thailand, The United States, Viet Nam	<p>As might be anticipated given U.S. participation in APEC, CPLG's mandate reportedly does not include contingent trade protection and replacing antidumping, subsidy/countervail and safeguards with competition rules (Hoekman (2002:12).</p> <p>All 21 members except for Brunei reportedly now have functioning competition laws and authorities; many of these were established in the past decade or so including: PRC, Hong Kong, Malaysia, Papua New Guinea, the Philippines, Singapore and Vietnam.</p> <p>For many of these countries, in addition to domestic pressures, the combination of the more formal ASEAN obligations and the soft law, moral suasion, and information based approach of APEC can take some credit for the significant expansion in functioning competition regimes in the Asia Pacific region over the past ten years.</p>
The Five "BRICS" Economies	Brazil, Russia, India, China and South Africa – South Africa joined in 2010	<p>The BRICS group of countries is an informal association of five emerging market economies which now meet annually for formal summits. The Brazil (BRICS) group of countries does not currently involve formal trade and commercial arrangements with competition policy and law obligations.</p> <p>However, media and other reports indicate that:</p> <ul style="list-style-type: none"> <li>(i) the BRICS relationship could become more formal and comprehensive at some point in the future;</li> <li>(ii) all five BRICS economies have functioning competition laws and authorities;</li> <li>(iii) and are clearly becoming leaders among the developing and emerging market economies that are now participating in various global and regional competition policy and law institutions, forums and networks.</li> </ul> <p>The BRICS have held four conferences on competition policy and law; and these conferences are now held every two years. The conference in November 2013 held in New Delhi India focused on competition law enforcement in the BRICS economies. The most recent conference from November 11-13 2015 took place in Durban South Africa and its theme was "Competition and Inclusive Growth". Some of the major topics included:</p> <ul style="list-style-type: none"> <li>(i) "Behavioural Economics and Its Meaning for Antitrust Agency Decision Making" by Professor William Kovacic of George Washington University;</li> <li>(ii) 'Behavioral Screening' and "Collusion and cartels: successes and challenges" by Professor Joseph Harrington of the University of Pennsylvania;</li> <li>(iii) "Unilateral effects in Mergers" and "Alliances and horizontal agreements" by Professor Tom Ross of the University of British Columbia;</li> <li>(iv) "The use and misuse of economic evidence" by Jorge Padilla of Compass Lexecon Europe;</li> <li>(v) "Perspectives on judging competition law cases: the role of economic evidence" by Professor Frederic Jenny (OECD);</li> <li>(vi) "The economics of antitrust sanctioning" by Professor Yannis, Katsoulacos of Athens University of Economics and Business;</li> </ul>

Regional Trade Agreement (RTA)	Member States (MS)	Formal and Informal Obligations of Member States (MS) under the RTA and Progress in Achieving Obligations and Objectives <sup>3</sup>
		<p>(vii) “Two sides of the same coin – how can the BRICS countries use the interplay between Competition law and Intellectual Property Rights to spur economic development?” led by Nelly Sakata;</p> <p>(viii) And other sessions on the interactions between competition and trade, competition and economic growth, competition and innovation, regional integration and competition policies, dealing with dynamic counterfactuals, and research and support for competition including the role of BRICS’ academic institutions.</p>

## Appendix B:

### Applying the Ten Questions in Sub-Section 4.2 to Proposals that the Southern Africa Development Community (SADC) Should Move Upscale and Adopt a Modified EU Model

Question	Rating from Low: One to High: Five	Comments on the Rating
1. How many MS have functioning competition laws and authorities and practical experience with case selection, investigation, analysis, and sanctioning anticompetitive business arrangements and practices?		11 of 15 MS have functioning competition policies, laws and authorities with expanding enforcement and related experience — including with cross-border mergers and anticompetitive conduct.
2. Are the larger MS with significant competition law experience fully supportive of the regional competition rules and authority – and therefore prepared to accept the perceived and actual loss of national sovereignty, independence and control over key markets and sectors?		Little interest and support from South Africa and no apparent interest from other non-COMESA members – which appear to recognize and understand the South African concerns.
3. How similar and different are the MS competition objectives, policies, laws, standards, functions and enforcement practices.  And how much convergence would be needed to reduce these differences and make regional rules and authorities functional and effective in achieving national and regional competition, market integration, and other objectives?		Organic convergence now taking place, differences in content of law, standards, enforcement practices and analytical methods are not substantive and consequential and are narrowing, and differences in SADC objectives of policies and laws are not large enough to represent major constraints to adopting a more centralized EU model.
4. Can this degree of alignment and convergence be achieved in the short to medium term to allow the regional rules and authority to be established and appropriately tested, evaluated, and modified where required, and placed on a positive trajectory?		Convergence and related trends in answering question three, and large and expanding number of MS with functioning competition laws and authorities, suggest that required convergence would take place in the medium term and would not be a major constraint to a more formal and centralized RTA regime based on a modified EU model.
5. Is there sufficient market integration and cross-border trade within the region to generate the number and quality of cross-border		Fairly low but with an upward trend as regional integration, trade, and investment flows expand with SADC economic growth and fuller

Question	Rating from Low: One to High: Five	Comments on the Rating
and regional enforcement cases and related matters needed for the RCA to develop experience, expertise, visibility, credibility and legitimacy among MS, CAs, businesses, and other stakeholders both within and outside the region?		implementation of the other provisions of the SADC agreements on trade, industrial policy, investment and other matters.
6. Is there reasonably strong empirical evidence that existing more informal bilateral and multilateral instruments between members have failed to deter, remedy and prevent some cross-border cartels, anticompetitive mergers, dominant positions, and other anticompetitive conduct?		No strong empirical evidence to date but some recognition that this risk could increase in the future – in terms of both frequency and consequences for trade, investment flows, and competition with members states and the total SADC region.
7. Has consensus developed on easy to understand and apply guidelines on the scope of regional versus national rules; and the allocation of cartel, merger and other enforcement and related matters between national and regional levels.  In order to minimize conflicts between jurisdictions and promote transparency, certainty, compliance and enforcement across the region?		Question 7 has been given minimal attention to date, consistent with answers to earlier questions.  But underlying issues are recognized and discussed by some SADC MS competition authorities and other ministries and agencies. In general though, the perspective is that current more informal model is sufficient and functioning in a satisfactory manner
8. Is the consensus on these guidelines and related issues on jurisdiction, enforcement practices and competencies, and extraterritorial application likely to be stable and sustained across MS, regional entities and other stakeholders?		However, sources and author's 2011 experience in SADAC suggest that consensus could be quite easily developed if political decision is made to adopt modified EU model.
9. Are the regional competition rules and functions on offer expected to support and help to achieve the broader economic, social and institutional goals of the regional community and its members on broader socioeconomic goals and objectives?		Links with broader socioeconomic goals and objectives given some attention by MS and the SADC Secretariat but not in the context of moving upscale to a more formal model with binding commitments and centralized enforcement.
10. Are the human resource and leadership skills, and MS financial, political and other commitments, needed to sustain a regional		Given the small budget allocated to the SADC competition and consumer policy and law budget which allows for only one contracted employee, this question is

Question	Rating from Low: One to High: Five	Comments on the Rating
regime, available now and in the future?		given the lowest rating and would be a significant risk if a political decision is made to adopt the more formal modified EU model.
<b>Comments on the Possible Overall Rating:</b> Would depend on the weights given to individual questions but the importance of and low ratings given to several questions including 2, 5, and 6 to 10 suggest that the overall rating would be no more than two. The higher ratings for the other four questions and the comments on some other questions regarding future trends suggest that in theory the overall rating could improve in the years ahead but this would remain theoretical without stronger interest and support from the SADC MS leader, South Africa, from the other more experienced non-COMESA members, and from the major leaders in the SADC Secretariat, and stronger evidence from the COMESA experience that a more formal model generates much greater net benefits compared with the current SADC model that as of 2011 when the SADC study was completed was and likely still is considered to be satisfactory and sufficient.		

*Sources:* Ireland (2012), Enabling Environments (2011) and Appendix A. As indicated in Appendix A, eight of the fifteen members of SADC are also members of COMESA. These eight members are: the Democratic Republic of the Congo, Madagascar, Malawi, Mauritius, Seychelles, Swaziland, Zambia and Zimbabwe; as well Tanzania is a member of the East African Community (EAC).

Based on the sources and the author's SADC experience and discussions with the head of the COMESA Competition Commission, the effect of overlapping membership on SADC MS support for adopting a more formal and centralized EU regional competition rules is not known at this time and is contingent on a number of factors including: (i) the success of the more formal, comprehensive an centralized COMESA model; (ii) problems that may emerge in the future regarding the more informal SADC model; and, (iii) the progress and success of the COMESA-EAC-SADC Tripartite Free Trade Area Agreement that was signed in June 2015, which includes Annex 07 on Competition Policy and Consumer Protection.

This Annex has twelve separate articles on: (i) the importance of fair competition; (ii) prohibition of anti-competitive business behaviour; (iii) determination of a dominant position; (iv) abuse of a dominant position; (v) prohibited practices; (vi) mergers and acquisitions; (vii) consumer protection; (viii) sanctions; (ix) implementation; (x) cooperation and exchange of information; (xi) tripartite competition policy and consumer protection forum; and, (xii) cooperation between national and regional authorities for competition.

See e.g. <http://www.sadc.int/news-events/news/comesa-eac-sadc-tripartite-free-trade-area-launched/>

<http://www.tralac.org/resources/by-region/comesa-eac-sadc-tripartite-fta.html> and

[http://www.tralac.org/images/Resources/Tripartite\\_FTA/](http://www.tralac.org/images/Resources/Tripartite_FTA/)

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## Endnotes

- 1 In this regard, RTA, competition and other scholars and practitioners should monitor the progress, achievements and possible limitations of MoU on Inter Regional Cooperation and Integration between the COMESA, EAC and SADC signed in 2011 which addresses enhanced cooperation and stronger coordination of competition policies in Article 5 – see: [www.atf.org.na/cms\\_documents/d22-tripartitetriparrtitemousignedversion.pdf](http://www.atf.org.na/cms_documents/d22-tripartitetriparrtitemousignedversion.pdf)
- 2 See Appendix B for a preliminary effort to apply the ten questions to the information collected and analysis conducted by the author in 2011 when conducting the EU TradeCom/Enabling Environments (2011) consulting assignment.
- 3 Throughout this paper and appendix, the term functioning or functional competition law and authority is used in the broad sense of some evidence of enforcement capability, action, progress, performance and success.
- 4 For example, the Canada-Chile Free Trade Agreement of August 28 2013 has Chapter J on competition, monopolies and state enterprises, which has the quite standard provisions and obligations on competition law, as follows:
  - “i. Each Party shall adopt or maintain measures to proscribe anti-competitive business conduct and take appropriate action with respect thereto as such measures will enhance the fulfillment of the objectives of this Agreement.
  - ii. Each Party recognises the importance of cooperation and coordination among their authorities to further effective competition law enforcement in the free trade area. The Parties shall cooperate on issues of competition law enforcement policy, including mutual legal assistance, notification, consultation and exchange of information relating to the enforcement of competition laws/policies in FTA.
  - iii. Neither Party may have recourse to dispute settlement under this Agreement for any matter arising under this Article.”

See Global Affairs Canada 2015 <http://www.international.gc.ca/trade-agreements-accords-commerciaux/agr-acc/chile-chili/chap-j26.aspx?lang=en>

See as well Global Affairs Canada on the Canada-European Comprehensive Economic and Trade Agreement (CETA) at <http://www.international.gc.ca/trade-agreements-accords-commerciaux/agr-acc/ceta-aecg/index.aspx?lang=eng> – which includes Chapter 19 which has more extensive and detailed competition policy and law obligations compared with the NAFTA competition chapter discussed earlier.
- 5 As noted earlier, throughout this paper and appendix, the term functioning or functional competition law and authority is used in the broad sense of some evidence of enforcement capability, action, progress, performance and success.
- 6 See for example The East African “East African Community to set up authority to push for free, fair trade” June 1 2015 <https://asokoinsight.com/news/east-african-community-to-set-up-authority-to-push-for-free-fair-trade/>
- 7 MoU on Inter Regional Cooperation and Integration Amongst COMESA, EAC and SADC, available at: [http://www.tralac.org/wp-content/blogs.dir/12/files/2011/uploads/MoU\\_Inter\\_RegionalCooperationIntegration\\_19\\_01\\_2011.pdf](http://www.tralac.org/wp-content/blogs.dir/12/files/2011/uploads/MoU_Inter_RegionalCooperationIntegration_19_01_2011.pdf)
- 8 See as well Economy & Politics “Antitrust and Competition Laws and Regulations in Nigeria” Monday 02, November 215 <http://www.economyandpoliticsng.com/articles/2816/-Proshare> – similar arguments could be made for Ghana which is another larger and more important African country with currently does not have a fully functioning competition law and authority (see e.g. Ellis et al 2010).

- 9 See e.g. Edwin Vanderbruggen, Nishant Choudhary, and Chris Sheridan (2015) “Myanmar’s New Competition Law: A Pitbull or a Paper Tiger?” VDB/Loi Client Briefing Note –March 08, 2015 indicating Myanmar’s new competition law is based on Viet Nam’s 2004 competition law [http://www.vdb-loi.com/wp-content/uploads/2015/03/VDB-Loi\\_Client-Briefing-Note\\_Myanmar-Competition-Law-Pitbull-or-Paper-Tiger\\_8Mar2015.pdf](http://www.vdb-loi.com/wp-content/uploads/2015/03/VDB-Loi_Client-Briefing-Note_Myanmar-Competition-Law-Pitbull-or-Paper-Tiger_8Mar2015.pdf)  
More recent media reports indicate that the Myanmar competition will become fully operational in February 2017 after more than a year of competition policy/law education and advocacy directed at the business community and other stakeholder groups.
- 10 Office of the United States Trade Representative “Summary of the Trans-Pacific Partnership Agreement” October 2015 <https://ustr.gov/about-us/policy-offices/press-office/press-releases/2015/october/summary-trans-pacific-partnership>



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As noted in the introduction to this paper, the author has attempted to bring together the very rich literature on RTA competition rules regimes, systems and outcomes with his personal experience and research on competition policy and law modernization and related regulatory reform initiatives within multi-country regional and global market contexts. For purposes of brevity and readability, specific references and citations are not provided in the main text. The following lists the articles, papers and studies that were reviewed when preparing this paper and had the greatest influence on its contents and arguments. The listing includes as well some of the author's studies, articles and conference presentations.

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# 16

## Competition Provisions in Trade Agreements

### *How to Realise their Potential?*

SEEMA GAUR  
*Adviser*  
*Department of Industrial Policy and Promotion*  
*Ministry of Industry and Commerce, Government of India*  
*India*

#### **Abstract**

It is widely recognised that the ongoing globalisation is considerably driven by trade and investment liberalisation. The lowering of trade and investment barriers,<sup>1</sup> and increased market access coupled with advances in international communication (including digital networks), transportation, finance, trade facilitation and knowledge-based services have led to increasingly interdependent economies in a global marketplace. Trade flows have grown in an unprecedented way alongside a sharp increase in foreign investment.<sup>2</sup>

In an environment where firms are increasingly organising their operations on a global scale and commerce is getting internationalised,<sup>3</sup> firms are more exposed to the regulatory systems (including competition law and policy) and business practices of different countries. Trade policy is not sufficient, on its own, to deal with the frictions that may result. Therefore, increasingly, trade agreements are being used to push for domestic regulatory liberalisation related to investment, competition and other key regulatory areas.

The international community has tried and tested various approaches to effectively tackle competition issues with a global dimension. They

include efforts to achieve a multilateral agreement within WTO, incorporating competition provisions within free trade agreements (FTAs), signing agency-to-agency bilateral agreements and informal cooperation between competition agencies.

This paper examines role of competition provisions within the framework of regional trade agreements (RTAs) and their effectiveness for cooperation. It draws on the existing research, discussions with scholars, practitioners and colleagues and personal experience of handling international competition cooperation and regional trade negotiations.<sup>4</sup>

## **Link between Trade Liberalisation and Competition Policy**

Trade and competition policy have a complementary relationship as both aim to improve efficiency of resource allocation, promote growth and enhance welfare, by keeping markets open and accessible whether it is by lowering governmental barriers to trade or through lowering barriers to competition. Consequently, both policies can be strongly pro-competitive<sup>5</sup> and pro-consumer, notwithstanding that one deals with government action at the border, the other with private action behind the border. Not surprisingly, it was during the period of increased liberalisation in the 1980s and 1990s that many countries enacted competition laws to ensure that the process of liberalisation leads to a more pro-competitive economic environment. Competition law and policy<sup>6</sup> provide essential tools for countering cartels, abuses of dominant position, and anticompetitive mergers that limit competition, impede development and thereby reduce economic welfare in developed and developing economies alike.<sup>7</sup>

Trade liberalisation can be a powerful tool for enhancing competition in many contexts.<sup>8</sup> On the other hand, as state barriers to trade and investment are being lowered, there are increasing concerns that the gains from this liberalisation may be thwarted by cross border private anticompetitive practices. This is because with the increasing integration of the world economy through trade liberalisation and expansion of foreign direct investment (FDI), abuse of market power has transcended national borders and acquired trans-border dimension affecting several nations.

Activities, such as international cartels and anticompetitive mergers pose a serious challenge to global welfare by curtailing potential trade and investment opportunities. It is critical for harnessing benefits of trade and investment liberalisation that such anticompetitive practices may be

checked through competition law and policy. The policy is also vital to ensure that international trade and global value chains operate in ways that are inclusive and open with respect to participation by all competitive suppliers<sup>9</sup> (Perez Motta, 2016).

## **Need for International Cooperation**

Globalisation has specific implications for competition law and policy. Alongside the growth in international trade and FDI, the number of cross-border mergers<sup>10</sup> and competition cases with a global dimension<sup>11</sup> (beyond the national jurisdiction)<sup>12</sup> has risen substantially. A purely domestic focus on competition policy is therefore no longer sufficient. The international nature of anticompetitive conduct opposed to the national jurisdiction of competition agencies implies a pressing need for international cooperation to effectively deal with the transnational competition law violations.

In the past two decades, competition law has gone global with its remarkable proliferation around the world.<sup>13</sup> This implies that as business increasingly globalises, same transaction or conduct may be subject to overlapping scrutiny by multiple competition authorities.<sup>14</sup> Consequently, this may lead to multiplication of costs for business and public exchequers, possible conflicting outcomes (including divergent remedies) and in some cases ineffective enforcement.<sup>15</sup>

This can have a chilling effect on legitimate business activity or (less likely) a freeing effect on harmful business activity with potential to impose additional costs on the global economy, and harm the consumers. Further, as more authorities<sup>16</sup> become more active in enforcement regarding global activity, lack of effective cooperation would increase the risk of application of substantive rules differently by various competition authorities over time. This implies a need for greater coordination of enforcement standards and remedies in competition law cases with transnational effects.<sup>17</sup>

Capobianco et al. (2016) observe that the purpose of international enforcement cooperation is twofold. Cooperation offers authorities the opportunity for more effective investigations and to generate efficiencies, for the authorities and affected businesses. Secondly, cooperation aims at minimising risks of divergent outcomes.

The evidence suggests that developing countries should also actively work for international cooperation in competition policy as a large share of competition problems of most developing countries emanates from the international sources such as import distribution monopolies and cartels; the influence of dominant firms based in other countries, including

neighbours; overseas export cartels; and regional market sharing.<sup>18</sup> This speaks of the great untapped potential in terms of North-South as well as South-South cooperation in competition policy enforcement.

## **Competition Provisions in Trade Agreements**

Regional integration is increasingly being recognised as an important means for promoting economic growth and reducing poverty and globally, FTAs have become a key instrument to achieve it. This is why; there has been phenomenon growth in FTAs in number and importance since the early 1990s. As effective trade liberalisation requires more than just a reduction of tariffs; FTAs are increasingly being used to address a host of behind-the-border domestic regulatory issues such as investment, competition, government procurement, environment and labour and human rights that may impact foreign trade.<sup>19</sup>

Although, most countries agree on strong relationship between trade and competition, they diverge on the merits, potential modalities, and even the necessity of adopting a multilateral competition framework.<sup>20</sup> Therefore, competition is no more on the multilateral agenda<sup>21</sup> and global attention has shifted to regional trade agreements.<sup>22</sup> Increasingly, competition provisions are being incorporated in negotiations for WTO-plus bilateral, sub-regional, and hemispheric agreements.

In a recent mapping exercise, Laprevote et al. (2015) found that out of 216 FTAs<sup>23</sup> reviewed by them, a substantial majority (88 percent) address competition-related issues in one form or another. This trend extends to FTAs concluded by developing countries, 87 percent of which included competition-specific chapters or provisions. The ongoing negotiations in the framework of the Trans-Pacific Partnership (TPP) and the Transatlantic Trade and Investment Partnership (TTIP) further illustrate the continuing importance of competition policy considerations in the context of modern trade negotiations and policy formulation (Anderson and Muller 2015).<sup>24</sup>

### **Why Competition Provisions in Trade Agreements?**

The question arises why competition related provisions are increasingly being incorporated in trade agreements. A most often quoted objective is to ensure that the benefits of trade and investment liberalisation are not compromised by cross-border anti-competitive practices. Competition chapters in FTAs are considered to be useful to act as a catalyst to bolster domestic support for competition policy (including adoption of competition law and its enforcement) in developing countries that domestic

interest groups otherwise might resist. They are also aimed at fostering cooperation in the area of competition enforcement to curb anticompetitive practices.

Further, new generation agreements focus more on economic integration than reduction of tariffs for which competition provisions are necessary structures.<sup>25</sup> Competition provisions in FTAs are also incorporated to create region-wide competition policies and institutions that seek greater levels of integration including, in the limit, forming common markets or economic and political unions.<sup>26</sup>

Further, Laprevote et al (2015) find that a limited proportion of the FTAs that contain competition-related provisions (6 percent) expressly describe the goal of these provisions in terms of broader economic objectives such as “economic efficiency and consumer welfare,” or “economic and social development”.

Competition provisions have been used by developed countries such as EU and the US to advance their trade interests. The literature suggests that the inclusion of competition provisions in trade agreements may be potentially beneficial for developing countries also as they are particularly vulnerable to intra-regional anticompetitive practices such as international cartels.

### **Key Provisions in Competition Chapters**

Literature review indicates that competition policy provisions in trade agreements can be of two types: a) those incorporated in chapters concerning state aid and enterprises, procurement, investment, intellectual property and also in terms of the core principles governing the RTA as a whole, such as transparency, non-discrimination and due process; and b) those covered as special chapter on competition policy. This section focusses on the provisions in the specific chapter on competition policy.

Diversity, it would seem, is the dominant attribute of provisions on competition law and policy<sup>27</sup> in trade agreements. Solano and Sennekamp (2006) find that FTAs take different approaches as to substantive competition rules and setting up of mechanisms on competition-related matters. Laprévote et al. (2015) also observe significant formal and linguistic differences between various approaches to addressing competition-related issues. They find competition provisions in FTAs ranging from ambiguous obligations through to deep commitments. At one end of the spectrum, there are provisions that lay out, in very broad terms, the obligation of promoting competition without further elaboration.

At the other end, FTA obligations are more clearly defined and involve detailed provisions relating to addressing anticompetitive practices and promoting cooperation amongst the parties. Further, Cernat (2005) noted that there are two sets of competition provisions that can be found in FTAs: provisions that provide for harmonisation of competition rules of the contracting parties such as EU bilateral FTAs, and/or provisions that provide for cooperation on competition-related issues such as bilateral RTAs signed by the US and Canada.

A review of relevant literature<sup>28</sup> indicates that broadly, competition provisions in FTAs cover a range of issues as briefly discussed below:

*i) Adopting and maintaining competition laws*

This category of provisions is particularly broad and diverse. While some FTAs contain rather vague obligations to adopt ‘measures’ or ‘laws’ against anticompetitive practices, many others define the anticompetitive practices to be regulated and/or the measures to be implemented to that effect, although the level of detail may vary. These practices cover (i) anticompetitive agreements, (ii) abuses of market power, and (iii) anti-competitive mergers.<sup>29</sup>

*ii) Competition enforcement principles*

Laprevote et al. (2015) note that only around 26 percent of FTAs<sup>30</sup> require the parties to enforce their competition laws in a transparent and non-discriminatory way and/or to ensure procedural fairness.<sup>31</sup> Mostly, they are supplemented by principles of procedural fairness, or, more rarely, timeliness, and comprehensiveness. By contrast, provisions requiring that the parties’ competition authority be independent are rare (two percent). There may also be special and differential treatment (S&DT) provisions in case of FTA parties being at different stages of competition development.

*iii) Regulating designated monopolies, state-owned enterprises and State aid*

One of the most common provisions<sup>32</sup> aims to address trade distortions and concerns over competitive neutrality resulting due to designated monopolies and state owned enterprises. While recognising the parties’ prerogative to establish and maintain such enterprises, these provisions aim to level the playing field to the extent practicable and display substantial variations in scope and language. Around 41 percent of the FTAs<sup>33</sup> contain provisions concerning the regulation of subsidies or state aid with varying levels of scope; and obligations.

*iv) Competition-specific exemptions*

Some FTAs allow the parties to either (i) implement competition-specific exceptions and exemptions provided they are transparent, undertaken on the grounds of ‘public policy or interest’ or being ‘no broader than necessary’ to achieve ‘legitimate policy objectives’; and/ or (ii) to carve out specific sectors that are already exempted from their domestic competition laws.

*v) Cooperation and coordination on competition*

Provisions on cooperation and coordination encompass a wide array of mechanisms, ranging from mutual legal and technical assistance, to notification, consultation, and exchange of information.<sup>34</sup> Mutual legal and technical assistance<sup>35</sup> may include assistance for ‘the provision of independent experts’ and for ‘training for key personnel,’ and help in drafting guidelines, manuals and, where necessary, legislation. Notification refers to duty to inform the other party of any enforcement activity that could affect the important interests of the other party. Consultation provide for the parties to consult with each other to eliminate particular anticompetitive practices affecting trade or investment amongst the parties. Exchange of information is typically limited to non-confidential and/or public information.<sup>36</sup> Several FTAs now also contain provisions on positive and/or negative comity, in which the parties agree to cooperate on a reciprocal basis in implementing mechanisms for competition law enforcement.<sup>37</sup>

*vi) Recourse to Trade Remedies*

The overwhelming majority of FTAs<sup>38</sup> allow the parties to resort to trade defences in one form or another (i.e. anti-dumping, anti-subsidy, and safeguard instruments), either by means of specific provisions or by reference to the corresponding General Agreement on Tariffs and Trade (GATT) rules.<sup>39</sup>

*vii) Dispute Settlement*

Competition provisions in FTAs have mostly been expressly exempt from the dispute settlement mechanism<sup>40</sup> of these FTAs.<sup>41</sup> In effect, the lack of dispute settlement has created soft law within the guise of a hard law agreement. Laprevote et al (2015) find that 47 percent of the FTAs in their sample set up competition-specific dispute settlement mechanisms, which usually take the form of consultation procedures. They oblige the parties, either by default or upon another party’s request, to consult with

each other to settle competition-related disputes, sometimes within a specific committee or in an inter-agency setting. At the deeper end of obligations, dispute resolution or consultation mechanisms could be provided for, or the creation of a supra-national authority that can apply competition law directly on private entities within the FTA (such as the EU, COMESA, CARICOM, the Andean Community, and Mercosur).<sup>42</sup>

Laprevote et al. (2015) found that the 190 FTAs that refer to competition policy in one way or other display numerous combinations of these provisions, with only one (European Union [EU]-Republic of Korea) including all of them. Thus, the provisions listed above are not cumulatively perceived by the contracting parties as indispensable components of a pro-competitive FTA<sup>43</sup>. Anderson and Evenett (2006) observe that the competition chapters of some RTAs appear to be as advanced, if not more advanced, in their provisions to foster cooperation between competition agencies on enforcement matters as second-generation inter-agency agreements between competition authorities. Relatedly, it is worth noting that the competition elements in many recent FTAs go well beyond the degree of cooperation that was envisioned in the proposals for a multilateral framework on competition policy in the WTO.

## **Indian Scenario**

India is still relatively less globally integrated and not an effective part of the global supply chains. Further, India does not want to be an island in the sea of ever-rising regionalism and suffer disadvantages for not being a part of the trend. Hence, India has been actively participating in FTAs and the Regional Comprehensive Economic Partnership (RCEP),<sup>44</sup> which is being presently negotiated.

India has been enforcing a modern competition regime since 2009. However, India is a late entrant to the specific competition provisions in its FTAs<sup>45</sup> as they were not included in its earlier trade agreements. With countries moving towards economic integration through FTAs, competition provisions are now demanded by developed countries like Japan, EU and Korea. India is also globalising at a fast pace with rising trade and investment interests in foreign countries, which require a level playing field. Further, the Competition Act, 2002 under Section 32 envisages extra territorial reach which may be facilitated by competition provisions in FTAs. In view of the above, they have now become integral part of all the recent Indian FTAs. The FTA with Korea was the first agreement which had a very simple version of a competition chapter.



Competition chapter is also included in Comprehensive Economic Partnership Agreement (CEPA) with Japan and is being negotiated in Broad Trade and Investment Agreements (BTIAs) with EFTA and EU as well as the RCEP with ASEAN and its trading partners. However, there is hardly any experience of cooperation amongst competition agencies based on the chapters in FTAs, although the Competition Commission of India has signed MOUs with some of the key jurisdictions and is in the process of signing with few others. Robust cooperation is taking place either within the framework of these MOUs or informally.

## Implementation of Competition Provisions in FTAs

### Implementation

Extensive UNCTAD work<sup>46</sup> on the subject shows that<sup>47</sup> despite various countries' eagerness to sign RTAs with competition provisions, there is very little experience concerning their implementation and their effectiveness with regards to improving competition. Sokol (2008) observes that until now, the effectiveness of competition policy chapters has remained unanswered. Gal (2012) finds that most regional competition agreements (RCAs) have yet to realise their potential. Almost all the newly sprung RCAs thus far have not significantly enhanced competition law enforcement in their regions, or have encountered serious difficulties in doing so. This empirical finding applies regardless of the region and the special characteristics of the jurisdictions within it. He goes to the extent of observing that rather, most do not justify their costs of creation and some even create negative welfare effects on their member states<sup>48</sup>.

Dawar and Holmes (2011) also argue that it is difficult to assess the implementation of competition provisions. Where it is possible, most existing research suggests that the level of implementation of regional competition provisions tends to be low, particularly in developing countries. This has led to questioning of the value of incorporating such provisions into FTAs, in view of the burdens of negotiating them and building institutions. But the research has also generated analyses that seek to identify and solve implementation challenges to harness the regional public goods that such provisions can potentially provide.

Laprevote et al (2015) observe that that the data collected by them does not allow for a solid assessment of the practical effects of competition-related FTA provisions. While several countries (for example, South Africa, Mexico, Canada) have reported that their FTAs including competition-related provisions contributed to "*the institutional*

*development and resulting capacity of their [competition] agencies*"<sup>49</sup>, further research is required to assess whether such provisions have stimulated the adoption or modernization of competition laws and enforcement.

Dawar and Holmes (2011) also find that in North-South agreements, the implementation record is somewhat better. Canada-Costa Rica, EU-Jordan, and EU-South Africa competition regimes have had some success in advocating a competition culture and in promoting cooperation between competition authorities through learning by doing. In North-North agreements, with fully centralised competition regimes such as the EU, the implementation record is better.

The existing evidence does not point to a 'one size fits all' approach. Approaches used by developed countries to deal with competition issue at regional level may not be relevant for FTAs among developing countries.<sup>50</sup> Studies indicate that most of the deeper regional competition systems such as in Latin America have mirrored the EU competition model, especially in relation to its substantive provisions. Nevertheless, with the exception of the EU, no other regional competition law system has so far proved to be successful in terms of enforcement results.<sup>51</sup>

Further, the creation of a supranational authority in a South-South agreement<sup>52</sup> raises a series of political economy problems in these settings which might make the implementation of regional competition provisions difficult.<sup>53</sup>

Sometimes, RTA cooperation on competition provisions in FTAs may be useful but informal cooperation may be more effective as seen in many cases. Most competition agencies utilise less formal agency-to-agency cooperation agreements<sup>54</sup> more often than complex state-to-state co-operation mechanisms in competition chapters in FTAs.<sup>55</sup> Informal relationships built up among competition enforcers through interactions at international meetings or technical cooperation or informal bilateral agreements also play an important role in practical cooperation.<sup>56</sup>

## **Lessons**

Question arises why implementation record has been so poor? What are the emerging lessons for future? This section attempts to answer these questions.

It may be mentioned at the outset that the fundamental problem arising from the implementation of substantive competition provisions in FTAs relates to the loss of policy autonomy, or space (UNCTAD 2013). This is accentuated in cases where the countries concerned have different levels

of development and hence widely diverging priorities. The underlying obstacle has been identified as the problem of supra-nationality,<sup>57</sup> that is, the relationship between regional and national laws.<sup>58</sup>

The weak implementation record can be partly explained by the fact that FTAs with Competition provisions are a relatively new phenomenon. The history of regional integration has shown that ‘deep integration’ rules, such as competition provisions, need time to fully materialise, particularly in FTAs involving developing countries.<sup>59</sup> Further, domestic competition enforcement and regional cooperation are correlated. Many developing countries still either lack a competition law or the law being of recent origin, they suffer from low institutional capacity of domestic competition institutions as well as weak competition culture impacting potential for cooperation.<sup>60</sup> Dawar and Holmes (2011) observe that in the absence of the requisite laws, institutions, and expertise, the country cannot absorb or take advantage of the benefits offered by provisions.

Further, several factors undermine cooperation under the competition chapter such as poor design of competition provisions, asymmetry of competition law development and capacity to enforce the law,<sup>61</sup> lack of requisite competition culture, lack of political will to promote domestic competition law enforcement and lack of mutual trust<sup>62</sup> among the competition authorities.<sup>63</sup> Significant legal and social differences between the parties compound the problem.<sup>64</sup>

There is wide heterogeneity of participating countries in terms of size, level of development or maturity of their competition systems or even existence of competition law. Since different legal and administrative systems and capabilities make a ‘one size fits all’ approach unsuitable, it may be a complex and challenging task to negotiate competition chapter agreeable to all the parties. UNCTAD (2013) findings suggest that involving competition authorities in the negotiation of an RTA might help to make the competition chapter more effective.

Gal and Wassmer (2012) suggest that while a basic understanding and national application of competition law is not a prerequisite for the success of regional competition agreements, a successful competition law regime, at least in some member states, can act as a catalyst to the adoption of competition agreement in FTAs and its successful operation. For one, the positive experience of some member states can serve as a basis for competition law advocacy. Second, the accumulated knowledge can be built upon in operating the agreement.

Gal and Wassmer (2012) argue that the benefits of regional competition provisions are determined, *inter alia*, by the modalities of cooperation on

which they are based. Obviously, the lower the level of proposed cooperation, the lower the potential benefits, but possibly also the lower the obstacles to its adoption and enforcement. Therefore, the level of cooperation should be determined with regard to the realistic capabilities of member states, including institutional weaknesses.

Sufficient resources (both financial and human) are an important precondition for an operational regional competition authority (RCA). Indeed, resource deficiency has plagued many RCAs.<sup>65</sup> Insufficient resources often result from wider macro-economic conditions in member states such as deep poverty, regional conflicts or natural disasters and competition law often is not a priority. This fact strengthens the need to determine, from the outset, whether indeed it is in a country's or a region's interest to invest in competition law. Yet, as studies show, there is often an economic justification for investing in competition enforcement to increase total welfare, and thus the question becomes one of sequencing and of governmental preferences of what to do first.

Lack of implementation of competition Chapters also may be attributable to the fact that the benefits of devoting efforts to cooperation are insufficiently clear and long term, while the costs are high and immediate.<sup>66</sup> The challenge is to craft the competition provisions so that the accruing benefits are seen to exceed the implementation costs. For developing countries, S&DT provisions may help achieve a proper balance between costs and benefits.<sup>67</sup>

### **Contribution**

Does the above analysis imply that RTAs have really no value?

Competition provisions in RTAs contribute to promoting international trade and investment by building transparent and predictable trade regimes. Introducing competition provisions in an FTA may signal 'a credible commitment to potential foreign investors that a country is market-oriented and pro-investment'. Conversely, 'the symbolic inclusion of competition policy within [F]TAs may create domestic legitimacy and assist competition agencies to pursue their competition enhancing missions' (Sokol 2008).

Further, as competition laws and policies are discussed during RTA negotiations, government officials, domestic and foreign companies, and the general public come to recognise the necessity of competition provisions in RTAs.<sup>68</sup> This can be expected to make a significant contribution to disseminating competition culture across the world in the long term.

One common trend that seems to emerge is that RTAs are a means of opening communication channels, which may be subsequently expanded

by the competition authorities until a satisfactory level of cooperation has been achieved. Also, it is important to note that the ‘domino effect’ of RTAs tends to spread competition legislation to new countries (due to conclusion of trade agreements having competition chapters), which may increase the opportunities for cooperation and experience sharing among competition authorities (UNCTAD 2015).

Gal and Wassmer (2012) observe that regional competition agreements have a potential to further the goal of a common, integrated market as demonstrated by the European experience of joint competition law enforcement. They might also increase certainty and compatibility of competition law enforcement either by transferring enforcement powers to the regional authority<sup>69</sup> or by adopting tools to increase compatibility between national competition laws. This, in turn, may strengthen incentives to enter and expand in regional markets.

Sokol (2008) further observes:

*In spite of the non-binding nature of competition policy chapters in RTAs, these chapters may still have value, which is related to how these chapters may help to identify, shape, and implement norms of competition policy in member countries. In the case of North-South agreements, they can help strengthen competition policy regimes in developing countries through technical assistance and capacity building support. However, their limitations need to be recognised. Should expectations for them be too high (given what they can deliver), and should negotiations over the inclusion of RTAs take up too many resources, the value of their exclusion may exceed the value of their inclusion.*

Thus, it is clear that in spite of poor implementation record, competition provisions in RTAs have value and substantial potential for promotion of competition law and policy in the region, provided their limitations are recognised.

### Limitations

Competition provisions included in FTAs belong to the category of soft laws as they are not legally binding and generally out of the purview of the dispute settlement mechanisms. Even the jurisdictions most committed to competition and free trade routinely exclude competition-related matters from their FTAs’ general dispute settlement mechanism.<sup>70</sup> They are based on best endeavour depending on the goodwill of the parties to have meaningful effect. This naturally makes them less effective;

however, soft laws may lead to increased compliance through norm creation.<sup>71</sup>

Exclusion of competition-related matters from the general dispute settlement mechanism<sup>72</sup> in numerous FTAs is a crucial weakness and raises concerns about the potentially purely symbolic nature of these provisions.<sup>73</sup> Because there are no minimum international obligations in competition law, countries may be less willing to give up sovereignty in this area, as they have not done so previously. This also illustrates the difficulties of agreeing to a binding multilateral framework. It may be worthwhile to consider whether international dispute resolution could be progressively introduced so as to elicit participation of national competition authorities.

Another critical element, which determines to a large extent the parameters and success of cooperation in competition law enforcement, is the definition and use of confidential information. Generally, competition provisions in FTAs place restrictions on exchange of confidential business information, which limits enforcement cooperation. The definition of confidential information, as well as its potential use may be studied. Despite the constraints imposed by confidentiality,<sup>74</sup> ways may be found for exchange of confidential information by providing for adequate safeguards against unauthorized disclosure.

## **The Way Forward**

In principle, competition provisions in RTAs can address market failures that national competition laws cannot and they can offset, to some degree, the absence of an international regime.<sup>75</sup> However, the available evidence<sup>76</sup> clearly shows that countries are eager to ink RTAs with CRPs but are far less eager to implement them.<sup>77</sup>

Despite limited evidence about the impact of the regional competition regimes, it is clear that lack of regional competition can undermine the benefits from liberalisation and integration of regional markets.<sup>78</sup> The need for competition law enforcement cooperation is driven by the increasingly interconnected nature of economic activity; and the increased number of jurisdictions enforcing competition law, and the increasing activity that can be expected from young/new competition authorities.<sup>79</sup> Hence, importance of international cooperation to ensure effective and coherent enforcement of competition laws around the world has never been greater or more complex to achieve.

Extensive UNCTAD work over the last decade<sup>80</sup> shows that there is a large untapped potential for cooperation under existing competition provisions in FTAs, the remaining barriers to cooperation should be explored and strategies to overcome them designed. Therefore, this section examines what steps can be taken to realise the beneficial potential of competition provision in FTAs.

Achieving favourable outcomes with competition provisions in FTAs requires that the provisions be well designed taking into account differences in the size, current socioeconomic conditions, level of economic development, legal developments and institutional capacity of each member state; have strong political and stakeholder support; and be effectively enforced within each member state. Ensuring the wide stakeholder participation in the development of a soft law instrument like competition chapter may be helpful in securing domestic support. The ICN experience shows that stakeholders are typically sympathetic to the ‘best practices’ approach.<sup>81</sup>

There should be clarity about the objectives to be achieved and their relative importance.<sup>82</sup> Goals should be set in relation to the conditions of countries in the region, the special competition law issues facing them, and the tools at their disposal to deal with such issues.<sup>83</sup> Competition law and policy work within the larger development context to create a more competitive environment and to encourage growth and productivity.<sup>84</sup>

Rather than focus only on preventing anticompetitive measures that may undermine the trade agenda, it is vital to emphasise the importance of competition policy to achieving economic development goals.<sup>85</sup> This may make the inclusion of competition provisions in FTAs more acceptable to developing countries.<sup>86</sup> Conversely, continuing to frame international competition policy as a pure market access issue may risk antagonising domestic constituencies in developing countries.<sup>87</sup>

Further efforts are needed in the actual process of chapter negotiations and the ways in which competition provisions are tailored to a specific agreement. It may be particularly useful to involve competition authorities<sup>88</sup> in the negotiation of competition chapters in FTAs.<sup>89</sup> This may enhance potential for effective cooperation in several ways: a) competition authorities get opportunities for repeated interactions over long periods of FTA discussions helping in fostering informal relations even before signing of FTAs; b) competition authorities are likely to negotiate provisions taking into account practical differences in their enforcement capacities, legal frameworks and other relevant factors; and c) provisions on technical cooperation and S&DT may be better designed based on realistic assessments of needs of less developed partners.

While it is true that competition policy can be a powerful policy tool, getting the benefits from effective competition policy involves human capabilities and specialised expertise. Strengthening human and institutional capacities in the weaker partners may provide a conducive politico-socio-economic environment in the countries to fully exploit the benefits of the competition provisions in FTAs and ensure a level playing field in international trade.<sup>90</sup>

Cooperation among agencies can be set at different degrees – from a low level (information sharing, technical assistance) to a high one (RJCA). Level of cooperation should be determined with regard to the realistic capabilities of member states, including institutional weaknesses.<sup>91</sup> In FTAs involving members with no or little experience with competition, it may be good idea to initially restrict the cooperation provisions to information exchange, technical assistance, and capacity building. More general commitments could be implemented after the necessary expertise and cooperation mechanisms have been developed. The inclusion of such an evolving clause allowing members to adopt a gradual approach to enlarge the scope of regional competition provisions would introduce additional flexibility in implementation and likely to enhance its potential for successful implementation.<sup>92</sup>

It may be useful to compare the impact of competition provisions in FTAs with other instruments used to promote cooperation, whether in terms of informal arrangements, bilateral agency-to-agency agreements (ATAs) or Mutual Legal Assistance Treaties (MLATs) where possible.<sup>93</sup> There may be merit in promoting direct inter-agency cooperation as a complement to regional competition provisions by signing direct agency to agency cooperation agreements.<sup>94</sup> This may be done either outside the competition chapter<sup>95</sup> or by providing in the competition chapter itself. Agency to agency agreements have better prospects for enforcement cooperation rather than state to state competition chapters, who may be more useful for creating support for competition policy in the domestic economies.

As to some extent, poor implementation also results from lack of dispute settlement, non-binding ways of dispute settlement such as consultations on issues relating to the implementation of agreements and diplomatic methods of dispute settlement such as conciliation, mediation and good offices in the context of international cooperation on competition policy may need to be incorporated in the competition provisions in FTAs.

For successful adoption of regional competition regimes in lesser developed partners, it may be useful to demonstrate benefits of cooperation



*vis-a-vis* its costs. Perez Motta (2016) suggests that to highlight and enhance the benefits of the adoption of a competition chapter among competition authorities and governments, it would be useful to: (i) precisely identify the key common areas of agreement in FTAs and reconcile the differences between approaches; (ii) increase awareness regarding the benefits of competition provisions in FTAs in order to reduce political costs; (iii) facilitate technical assistance<sup>96</sup> to states that face difficulties in implementation; and (iv) assess the potential trade concessions that might be needed to incorporate competition clauses in FTAs.

Further research is needed on economic and development impact of regional competition law and policies. There is need to understand various issues such as whether effective cooperation instruments can be designed for regional integration in the absence of effective institutional powers? How much co-operation is going on under formal provisions and how much informally? Whether competition provisions have fostered cooperation between agencies on actual enforcement cases? What are the impediments to co-operation? What disputes have arisen on competition provisions in FTAs between signatories of agreements? How were they solved? What are the pros and cons of binding competition enforcement and so on?

It may be pointed out that very significant progress in promoting better understanding of the objectives, modalities, and effects of competition policy around the world has been made as a result of work undertaken by international organisations such as the ICN, the OECD; and UNCTAD, in addition to national competition agencies and non-governmental organisations (NGOs) such as CUTS.<sup>97</sup> Developing economies have now far greater practical experience with the application of competition policy,<sup>98</sup> reflecting the capacity building that has taken place and the proliferation of competition laws across such countries in recent years.<sup>99</sup>

Further, increasingly frequent inclusion of competition policy provisions in FTAs and their overall substantive convergence as regards the most basic principles suggest that there may be fertile ground for international harmonisation in the form of a model FTA competition chapter.<sup>100</sup>

Perez Motta (2016) argues that in addition to fostering further cooperation and convergence in enforcement matters, future or presently negotiated trade and investment arrangements could act as a vehicle for incremental harmonisation of competition laws and practices in the absence of an international agreement on these issues.<sup>101</sup>

Capobianco et al (2016) even suggest that if jurisdictions can adopt common approaches both to enforcement itself and the cooperation, it

makes sense to embed these in a multilateral instrument rather than a plethora of bilateral agreements.

To conclude, cooperation under competition provisions in FTAs has so far been quite low but it is slowly growing. The fact that there is discourse on further minimising differences between competition regimes through platforms like ICN is indicative of further enhancement of the level of cooperation. Given significant progress in promoting understanding of benefits of competition policy and developing common approaches towards competition enforcement as well as capacity building even in developing countries, better implementation of regional competition provisions can be expected in future.

However, there is need to understand that the extent to which a regional competition regime can deal with market failures depends largely on the appropriateness of design of the provisions and the will of the parties to enforce them. Expeditious progress can be achieved if strengthening of implementation capacity in developing and transition FTA members is accompanied by reinforced commitment from developed members to effectively address the competition policy concerns of their trading partners. Finally, neither trade nor competition policy tools can provide complete solutions to the problems that emanate from the mix of governmental and private anticompetitive restraints.

## Endnotes

- 1 Barriers to trade and foreign investment have declined in developed and developing economies alike.
- 2 Perez Motta 2016. Since the 1990s, world merchandise trade has risen more than 500 percent. According to OECD 2014 estimates, total foreign direct investment (FDI) expanded more than four times between 1990 and 2012.
- 3 *Ibid.* Multinational enterprises (MNEs) have become global players and in their search for the best possible conditions, they have distributed their production and distribution activities worldwide.
- 4 The author was economic adviser and head of capacity building and international cooperation division at the Competition Commission of India (CCI) since it started implementing the law in May 2009 and worked till 2015.
- 5 Trade liberalisation results in an influx of goods into the economy, which could also have a huge impact on the nature and extent of competition in the markets, and encourage domestic competition as well.
- 6 The broader term “competition policy” encompasses, in addition to competition law, other measures that governments take to remove unnecessary structural or regulatory barriers to competition and promote healthy competition in markets.
- 7 Perez Motta 2016.
- 8 Anderson and Müller 2013. For example, in both primary products markets and service industries with limited possibilities for competition involving purely domestic players.
- 9 Competition law and policy can help add value to exports from developing and least-developed countries (LDCs) by removing barriers to key sectors in GVCs, OECD, WTO and World Bank Group 2014.
- 10 Capobianco et al. 2016. There are already situations today where 15 authorities from different jurisdictions are notified of the same merger for approval under their national law, and in many cases five or more authorities act on a merger. If 15 different authorities are reviewing the same transaction and if they need to cooperate bilaterally in their national reviews, the number of possible interactions would be more than a hundred.
- 11 *Ibid.* The number of cross-border cartels revealed in an average year has increased substantially since the early 1990s, mainly reflecting the increased use of leniency programmes. According to the Private International Cartel (PIC) database, about 3 cross-border cartels per year were revealed via competition authority decisions or prosecutions during 1990 -1994. During 2007 to 2011, an average of about 16 cross-border cartels has been revealed per year reflecting a 527% increase in cross-border cartel enforcement between 1990-4 and 2007-11.
- 12 *Ibid.* Cases and investigations reflect the increasingly cross-border activities of businesses and often require support from foreign enforcers.
- 13 *Ibid.* From 23 jurisdictions in 1990 to about 127 jurisdictions as of October 2013.
- 14 *Ibid.* Around two-thirds of the merger decisions by the Competition Commission of India in its first three years of merger review had an international dimension.
- 15 *Ibid.*

- 16 For example, during June 2011- March 2015, India issued decisions for 236 merger reviews. Source: Annual report 2014-15, Competition Commission of India, [www.cci.gov.in](http://www.cci.gov.in).
- 17 Supra Note 6
- 18 Utton 2008.
- 19 Sokol 2008.
- 20 Hufbauer, and Kim 2009.
- 21 Anderson and Muller 2015. Interaction between trade and competition policy was an important element of Doha round of multilateral trade negotiations. However, at 2003 Cancún Conference, majority of WTO Members rejected launching negotiations on a multilateral framework on competition policy. Hence, General Council of the WTO in 2004 decided not to undertake further work on competition policy. India also like many other developing countries did not support the multilateral agreement on competition policy.
- 22 This trend appears to have accelerated following the suspension of work in the WGTCP.
- 23 FTAs included in the WTO's RTA database – by far the largest sample of FTAs analysed. Solano and Sennekamp (2006) analysed 86 trade agreements that include competition related provisions, and found that about two thirds were between developing countries (often referred to as South-South agreements), and more than a fourth covered signatories from developing and industrialised economies (so called North South agreements)
- 24 Laprevote et al. 2015. They may also provide additional opportunities to extend the geographic scope of such provisions and perhaps even bolster a renewed effort to put competition policy back on the multilateral—or at least plurilateral—trade agenda
- 25 For example, Competition is an important aspect of ASEAN's vision of regional economic integration and competition law/policy is an essential instrument
- 26 UNCTAD 2005, Executive Summary
- 27 UNCTAD 2005.
- 28 UNCTAD 2005, OECD 2006, Sokol 2008, Teh 2009 and Laprevote et al.2015.
- 29 Provisions relating to anti-competitive mergers are significantly less frequent in FTAs than provisions covering cartels or abuses of market power. Only 11 percent of the FTAs in Laprevote et al. 2015 address anti-competitive mergers. Generally, they are FTAs to which highly advanced economies with significant merger control experience such as Australia, the EU, EFTA (or one of its Member States), Canada, Korea, New Zealand, or Singapore are party.
- 30 In their sample of 216 FTAs.
- 31 Some of the agreements including enforcement principles such as non-discrimination, transparency, and procedural fairness are indeed quite recent.
- 32 Found in 50 percent of Laprevote et al. 2015's sample pf 216 agreements.
- 33 41% of Laprevote et al. (2015) sample of 216 FTAs.
- 34 Refers to exchange of information between competition agencies.
- 35 Mostly included in North South agreements ( between developed and developing countries).

- 36 Generally applicable to the extent permitted by the parties' respective domestic laws.
- 37 *Supra* Note 6
- 38 Laprevote et al. 2015.
- 39 A very small minority of FTAs, namely the ANZCERTA, EFTA-Chile, EFTA-Singapore, EFTA-Serbia, and Canada-Chile preclude the parties from resorting to trade defenses and replace them with competition provisions.
- 40 The goal of dispute settlement is to ensure compliance with the rules laid down in the FTA.
- 41 Laprevote et al. 2015.
- 42 UNCTAD 2015.
- 43 That being said, it is worth noting that nearly 30 percent of the FTAs of Laprevote et al. (2015) sample include a combination of provisions relating at least to (i) anti-competitive agreements, (ii) abuse of market power, and (iii) designated monopolies and SoEs.
- 44 Regional Comprehensive Economic Partnership (RCEP) is a free trade agreement being negotiated amongst 16 Asian countries – 10 ASEAN Member States and ASEAN's 6 FTA partners- Australia, China, India, Japan, Korea and New Zealand. RCEP is intended to broaden and deepen current engagement that has already been achieved through the existing ASEAN+1 FTA.
- 45 Sahu and Gupta 2007. The study commissioned by CCI suggested that India could be benefited by including competition clauses in its future trade agreements.
- 46 Based on empirical evidence.
- 47 UNCTAD 2005, UNCTAD 2007, UNCTAD 2013 and UNCTAD 2015.
- 48 Weik 2010. The Senegalese experience provides an example. Due to WAEMU regional agreement, which Senegal joined, the Senegalese authority ceased to operate several years ago, but WAEMU has not as of yet created a viable alternative.
- 49 Mathis 2011.
- 50 UNCTAD 2015.
- 51 Botta 2011. Based on case studies of Mercado do Sur (Mercosur), Comunidad Andina (Andean Community, CAN) and the Caribbean Community (CARICOM).
- 52 When the countries involved have different levels of development in terms of their competition enforcement, for example CARICOM, MERCOSUR, Andean Community, Common Market for Eastern and Southern Africa (COMESA) etc.
- 53 UNCTAD2013.
- 54 Bilateral cooperation agreements result in more concrete and effective cooperation than RTAs' as they take into account differences between the two parties in level of development of their respective competition laws and policies.
- 55 APEC 2007.
- 56 Today, most competition authorities around the world speak the same economic and legal competition language, and enforce competition laws using comparable tools and principles.
- 57 Jenny and Horna 2005.
- 58 Alvarez et al. 2007. What is required is that 'the benefits of effective enforcement against anti-competitive practices with cross border implications (spillover effects)

and the gains from economic integration must exceed the loss of domestic sovereignty' for each country.

59 Cernat 2005, UNCTAD 2015.

60 An agency with a deep knowledge of domestic competition law enforcement - both in terms of procedure and of substantive aspects of the law - is better able to make use of the international instruments for cooperation.

61 Such as level of independence and resources of competition authority.

62 For example, in case of divergent merger regulations or leniency programmes, where more experience and greater institutional development are required.

63 For example, Brazil and Argentina.

64 UNCTAD, 2007 and Dawar and Holmes, 201.

65 For example, although COMESA has a Competition Commission, it cannot make decisions because of insufficient funding needed in order to employ the necessary staff.

66 Costs will essentially depend on human resources and expertise as well as financial resources needed to implement the various CRPs. Benefits stem from the ability to use CRPs in RTAs to curtail intra-RTA anticompetitive practices, such as international cartels. For developing countries, S&D treatment may help achieve a proper balance between costs and benefits.

67 UNCTAD 2015. A delay, exemption or technical and financial assistance in implementing a FTA's competition obligations would reduce the effective cost.

68 Asia Pacific Economic Cooperation 2007.

69 For example, filing of a request to merger firms that operate at the regional level only to the regional authority.

70 Laprevote et al. 2015.

71 Supra Note 19

72 Alvaarze et al. 2007. There are two goals for dispute settlement in competition within the context of an FTA : i) to ensure that partner country maintains commitments set out in the FTA; and ii) to ensure that positive comity can be enacted within the framework of the FTA to prosecute perpetrators of restrictive business practices in foreign territories.

73 Laprevote et al.2015.

74 UNCTAD 2007 (Chapter 1).

75 Dawar and Holmes 2011.

76 UNCTAD work as well as other work discussed in this chapter earlier.

77 Cernat 2005, UNCTAD 2007 and UNCTAD 2015.

78 Dawar and Holmes 2011.

79 Cabianco et al. 2015.

80 UNCTAD 2005, UNCTAD 2007 and UNCTAD 2013.

81 Laprevote et al. 2015.

82 Gal and Wessmar 2012. For example, is the goal economic development of members by removal of trade and investment barriers or is it integration and the creation of a common market.

- 83 *Ibid.*
- 84 Porter 2004
- 85 Evenett 2005
- 86 For example, EU-Overseas Countries and Territories FTA, which emphasises the importance of competition to development and industrialisation
- 87 Supra Note 19
- 88 For example, in the US, the US antitrust agencies are centrally involved with the negotiation of the text of the competition chapter.
- 89 The author as economic adviser at the CCI (2009-2015) was the lead negotiator on competition chapter from Indian side in several rounds of RCEP presently under negotiation. Other parties too had mostly negotiators from the competition authorities.
- 90 UNCTAD 2013.
- 91 Gal and Wassmer 2012.
- 92 UNCTAD 2007, Dawar and Holmes 2011.
- 93 UNCTAD 2007. For instance, whether the inclusion of competition-related provisions (CRPs) in RTAs leads to the signing of dedicated legal instruments for cooperation on competition matters.
- 94 Dawar and Holmes 2011.
- 95 The Competition agencies of India and EU signed bilateral Memorandum of Understanding for cooperation in 2013, while competition chapter in the trade agreement between the two countries is still under negotiation.
- 96 Need based tailor-made technical and capacity-building assistance to strengthen the institutional and enforcement capacity of less developed partners.
- 97 Anderson and Muller 2015.
- 98 Supra Note 6
- 99 *Ibid.* whereas during 1997 to 2004 (when competition policy was active on Doha agenda), an estimated 40–50 WTO Members had active national competition regimes, current surveys cite 110–120 countries having such laws.
- 100 Laprevote et al. 2015.
- 101 Among the various possible fora for carrying out such an undertaking, the ICN stands out as the only international platform that has both the needed flexibility and ability to influence policymakers

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**Consumer Unity & Trust Society**

D-217, Bhaskar Marg, Bani Park, Jaipur 302 016, India

Ph: 91.141.228 2821, Fax: 91.141.228 2485

Email: [cuts@cuts.org](mailto:cuts@cuts.org), Website: [www.cuts-international.org](http://www.cuts-international.org)